90-692

Supreme Court, U.S.
FILED
OCT 24 1990
JOSEPH F. SPANIOL, JR.
CLERK

NO. _____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

VICTOR ROGERS and LOREN SINGLETARY,
Petitioners,

v.

THE FEDERAL DEPOSIT INSURANCE CORP., As Receiver for FIRST REPUBLICBANK HOUSTON, N.A., and NCNB TEXAS NATIONAL BANK,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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October 19, 1990

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QUESTION PRESENTED

Whether the federal common law *D'Oench, Duhme* doctrine shields the FDIC and the successor to a failed financial institution from federal securities law claims —particularly claims under § 29 of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc?

RULE 28.1 LIST OF PARTIES

The original parties to the proceedings below included the petitioners Victor Rogers and Loren Singletary and the respondents the Federal Deposit Insurance Corporation ("FDIC") as Receiver for First RepublicBank Houston, N.A., and NCNB Texas National Bank ("NCNB"). Plaintiffs/Counter-Defendants/Appellants below Wade A. Kilpatrick and Stan E. Golub filed suggestions of bankruptcy and the counter-suit by the FDIC and NCNB was stayed as to them. Plaintiff/Counter-Defendant/Appellant Richard Howard is not pursuing this petition. Defendant/Counter-Plaintiff/Appellee below John C. Riddle filed bankruptcy and the plaintiffs' suit was stayed as to him. Messrs. Kilpatrick, Golub, Howard, and Riddle are not parties to this Petition.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Petitioners Victor Rogers and Loren Singletary respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit, entered in the above-entitled proceeding on July 25, 1990, and to resolve a conflict between the United States Court of Appeals for the Fifth Circuit, and the Fourth, Sixth, Eighth and Eleventh Circuits regarding preclusion of federal securities law claims by the federal common law *D'Oench, Duhme* doctrine.

OPINIONS BELOW

The opinion of the Court of Appeals for the Fifth Circuit is reported at 907 F.2d 1523 and is reprinted in the appendix hereto at 1a, *infra.*

The memorandum decision of the United States District Court for the Southern District of Texas (Hittner, D.J.) has not been reported. It is reprinted in the appendix hereto at 28a, *infra.*

JURISDICTION

The judgment of the Court of Appeals was entered on July 25, 1990. Rehearing en banc was denied per curiam on August 21, 1990. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

12 U.S.C. § 1823(e)

15 U.S.C. § 78cc

The text of the foregoing statutes is reprinted in the appendix hereto at 36a, *infra.*

STATEMENT OF THE CASE

1. Statement of facts.[1]

In 1983, John C. Riddle ("Riddle") and Jeffries C. Suttles ("Suttles"), debtors of RepublicBank Houston,

1. This case has never been tried on the facts. It was decided by summary judgment on the legal question whether the federal common law *D'Oench, Duhme* doctrine precludes the federal securities laws claims and defenses of debtors of failed financial institutions. Petitioners' federal securities fraud claims were taken as admitted for purposes of summary judgment.

N.A. ("RepublicBank") to the extent of tens of millions of dollars, embarked on a master plan to form a group of as many as five banks with financing from RepublicBank. Riddle and Suttles planned ultimately to consolidate all five banks under a holding company and then sell control of the holding company or the individual banks to RepublicBank. Pursuant to the master plan, RepublicBank agreed to finance the entire capital formation of both Texas National Bank-Post Oak ("TNB-Post Oak") and Texas National Bank-Westheimer ("TNB-Westheimer"), the only banks, as it transpired, which were formed under the scheme. To this end, RepublicBank financed the purchase of all stock in TNB-Post Oak to individual investors through loans procured by Riddle and Suttles. Subsequently, RepublicBank financed the purchase of stock in TNB-Westheimer through a master loan to Riddle and Suttles, who in turn reloaned the money to stock purchasers who were required to sign guaranties guaranteeing payment of 115% of their individual portion of the master loan. Petitioners purchased stock in both banks. Their claims for fraud and the notes executed to purchase stock in TNB-Post Oak and TNB-Westheimer as part of that fraud are at issue in this case.

As a final facet of the financing scheme, Riddle, Suttles, and RepublicBank required all directors and executive officers in TNB-Post Oak and TNB-Westheimer, as a condition of their election or appointment, to purchase bank stock whose voting powers were subject to a voting trust. Petitioners were both outside directors of the banks and were therefore required to purchase stock subject to the voting trusts. The voting trust for each bank gave complete voting power over stock subject to the trust to the trustees—Riddle and Suttles—as agents and granted

the trustees exclusive power to modify or terminate the voting trust agreement. Moreover, each voting trust agreement stipulated that should stock subject to the voting trust, including the trustees' stock, be transferred, it would remain subject to the voting trust, and therefore retain its control or non-control status.

The immediate effect of each voting trust was to vest exclusive control of both banks in Riddle and Suttles. The ultimate effect of the financing scheme for TNB-Post Oak and TNB-Westheimer, together with the voting trusts, was to give RepublicBank the option of going ahead with the master scheme or withdrawing from that scheme whenever it chose to do so and of either gaining control of those banks already formed, should it so desire, or simply abandoning them without capital cost or risk to itself. Given the heavy indebtedness of Riddle and Suttles to RepublicBank, RepublicBank could acquire control of TNB-Post Oak and/or TNB-Westheimer at any time, simply by demanding payment from Riddle or Suttles on the master note for TNB-Westheimer. Because of the voting trust agreements, it would not be necessary for RepublicBank to purchase the stock of the innocent investors in order to gain control of TNB-Post Oak and/or TNB-Westheimer, should it so desire. Thus, any benefit from the formation of TNB-Post Oak and TNB-Westheimer would accrue to RepublicBank—either in the form of affording Riddle and Suttles access to funds to pay off (however illegally) their massive indebtedness to RepublicBank or in the form of creating a successful bank acquisition if all went well despite all odds—while any losses could be transferred to the innocent investors through their personal notes and guaranties to RepublicBank.

In actuality, while fully aware of its own secure position through its control of Riddle and Suttles and its manipulation of the financial scheme for TNB-Post Oak and TNB-Westheimer, and also while fully aware of the precarious financial position of Riddle, Suttles and, later, TNB-Westheimer, RepublicBank encouraged and financed large bank stock purchases by the innocent investors, including Petitioners, at amounts well above book value, and continued to do so while the actual value of the stock was dramatically eroding. RepublicBank benefitted by creating new banks to which Riddle's and Suttles' debt could be moved, lessening RepublicBank's exposure. Riddle and Suttles, meanwhile, were manipulating TNB-Westheimer and TNB-Post Oak to their benefit.

Early in 1987 the scheme collapsed. Numerous incidents of self-dealing and straw loans by Riddle and Suttles to their cronies were uncovered by regulators (including the FDIC) and by the directors and investors in TNB-Westheimer. At or about that same time, Riddle and Suttles—who entirely controlled the voting stock in both TNB-Post Oak and TNB-Westheimer, but who had never paid anything on the master note for TNB-Westheimer—were discovered to have defaulted. Some of the defrauded directors and investors in TNB-Westheimer promptly brought suit on behalf of TNB-Westheimer against RepublicBank, TNB-Post Oak, Riddle, and other insiders of TNB-Westheimer in May, 1987. C.A. No. H-87-1552, *Texas National Bank-Westheimer, David R. Bolton, H.L. Hensen Murchison, Jr., William P. Plyer, and Seth J. Rilkin v. Texas National Bank-Post Oak, Walter E. Beard, Victor C. Bane, John C. Riddle, RepublicBank Houston, N.A., Fidelity Federal Savings Bank, and Vernon Federal Savings and Loan* (*"Bolton v. Beard"*). That same month,

TNB-Westheimer failed and the FDIC assumed control as receiver. The FDIC immediately intervened in *Bolton v. Beard* and vigorously prosecuted TNB-Westheimer's securities fraud claims against the defendants in that cause of action, including RepublicBank.

2. Proceedings.

In May, 1988, Petitioners, as stockholders of TNB-Westheimer and TNB-Post Oak, filed this action in federal court. They let this suit lie dormant, however, while they attempted to intervene in *Bolton v. Beard* as Plaintiffs on the side of the FDIC urging virtually identical fraud claims to those the FDIC itself was pressing against RepublicBank and the other Defendants. On July 30, 1988, RepublicBank in turn failed, and certain of its "assets," including Petitioners' notes, were sold by the FDIC to North Carolina National Bank—Texas ("NCNB") —a bridge bank formed to replace RepublicBank. The TNB-Westheimer directors and investors had meanwhile withdrawn their federal suit against Riddle, RepublicBank, and others and refiled in state court, leaving only the FDIC, as receiver of TNB-Westheimer, to prosecute *Bolton v. Beard.* The district court ultimately denied Petitioners permission to intervene in *Bolton,* given the FDIC's claims that it was close to a settlement with itself and that the presence of intervenors would complicate the suit.

When their intervention in *Bolton* was denied, Petitioners activated this suit. In place of RepublicBank they substituted the FDIC and NCNB as defendants in an amended pleading. The FDIC and NCNB, represented by the same attorneys who had appeared for RepublicBank in *Bolton,* counterclaimed in this suit and moved

for summary judgment on Petitioners' notes, claiming that the *D'Oench, Duhme* doctrine precluded all of Petitioners' claims for federal and state securities fraud, civil conspiracy, state statutory fraud, and common law fraud. The District Court granted Respondents' motion and entered final summary judgment in favor of the FDIC and NCNB on July 27, 1989. *See* app. 23a-33a.

A three-judge panel of the Fifth Circuit heard oral argument on March 5, 1990, and handed down its opinions on July 25, 1990. App. 1a-22a. The majority held that the *D'Oench, Duhme* doctrine,[2] which protects the FDIC from secret agreements between a failed financial institution and its customers, precluded not only Appellants' common law and state securities law claims but also their federal securities law claims, specifically their claims for damages under § 10(b) of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. § 78j, Rule 10b-5, and § 12(2) of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. § 771, and their claims for rescission of their contracts with RepublicBank under § 29 of the 1934 Act, 15 U.S.C. § 78cc. Slip op. at 12, app. at 11a.

The majority of the hearing panel acknowledged that only one federal appeals court had expressly rejected federal securities law claims on the basis of the *D'Oench, Duhme* doctrine.[3] The Court also acknowledged that two previous Circuit Courts had refused to extend the *D'Oench, Duhme* doctrine to federal securities law claims.[4]

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2. The *D'Oench, Duhme* doctrine was originally promulgated in *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 62 S. Ct. 676 (1942).

3. *FDIC v. Investors Assocs. X, Ltd.*, 775 F.2d 152, 156 (6th Cir. 1985).

4. *Gunter v. Hutcheson*, 674 F.2d 862 (11th Cir. 1982), and *Gilman v. FDIC*, 660 F.2d 688 (6th Cir. 1981).

Id. However, the Court held that the United States Supreme Court in *Langley v. FDIC,* 484 U.S. 86, 91-92, 108 S. Ct. 396, 401 (1987), extended the *D'Oench, Duhme* doctrine to preclude Petitioners' defenses, which it recast as fraud in the inducement. Slip op. at 9, app. at 8a. Judge Brown filed a dissent. Slip op. at 17, app. at 15a. This application thus poses a narrow but highly important point: whether the specific investor protection provisions of the Securities Exchange Act of 1934 take precedence over or are subordinate to the generalized treasury-protection impetus of the federal common law doctrine originated in *D'Oench, Duhme.*

REASONS FOR GRANTING THE WRIT

I. THE FIFTH CIRCUIT'S PRECLUSION OF FEDERAL SECURITIES LAW CLAIMS BY THE FEDERAL COMMON LAW *D'OENCH, DUHME* DOCTRINE STRETCHES FEDERAL COMMON LAW BEYOND PERMISSIBLE LIMITS.

A. The Fifth Circuit Opinion in this Case Recasts Federal Securities Law Claims as Common Law Claims.

D'Oench, Duhme estops the maker of "an instrument which is in form a binding obligation" from pleading that the instrument should not be enforced by the FDIC because of a secret oral agreement. 315 U.S. at 459, 62 S. Ct. at 680. The majority of the hearing panel in this case, relying on *Langley v. FDIC,* 484 U.S. 86, 106 S. Ct. 396 (1987), held that a unilateral misrepresentation by a financial institution to a borrower as to the

truthfulness of a warranted fact constitutes a secret agreement between the borrower and the bank to the effect that the instrument will not be collected if it was fraudulently induced and is therefore precluded by *D'Oench, Duhme*. Slip op. at 9,[5] app. at 8a.

Judge Brown, in his dissent, points out the essential flaw in the majority's argument. Petitioners' securities fraud claims are simply *not* based on *fraudulent inducement* to sign a contract—a common law claim which derives essentially from oral misrepresentations about the terms of a contract—*but* on the *fraudulent sale* of securities—a federal statutory claim specifically designed to protect stock purchasers from unscrupulous sellers and promoters of the stock. *See* slip op. at 8 (Brown, J., dissenting), app. at 21a. Judge Brown implicitly recognized that the majority's interpretation of *D'Oench, Duhme* requires a double recasting of Appellants' claims—(1) a recasting of fraud as an "agreement" and (2) a recasting

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5. The panel majority applied *Langley*, a 28 U.S.C. § 1823(e) case, to this case on the theory that § 1823(e) "codifies" *D'Oench, Duhme*. Slip op. at 1 ,app. at 1a. Though often repeated, the codification is not strictly correct. Prior to the enactment of the Financial Institutions Reform Recovery and Enforcement Act of 1989 ("FIRREA"), effective date August 9, 1989, the Fifth Circuit expressly held that § 1823(e) did *not apply to* cases such as the instant case in which the FDIC was involved as receiver of a failed bank, but only to cases in which the FDIC was involved in its corporate capacity, i.e., as the holder of notes issued by the failed financial institution. *See* 12 U.S.C. § 1823(e); *Beighley v. FDIC*, 868 F.2d 776, 783 (5th Cir. 1989); *FDIC v. McClanahan*, 795 F.2d 512, 514 (5th Cir. 1986).

Section 1823(e) provides that "[n]o agreement which tends to diminish or defeat the interest" of the [FDIC] shall be valid against the Corporation "unless in effect, it is spread all over the books of the defunct financial institution." Since § 1823(e) and *D'Oench, Duhume* are often construed together, a copy is attached at app. 31a.

of the fraudulent sale of securities under federal statutes as common law fraudulent inducement to sign a contract. The majority's extremely broad interpretation of *D'Oench, Duhme* thus goes far beyond *Langley* to require an interpretation of a fraudulent stock sale as a secret agreement between the victims and the perpetrators of the fraud. As Judge Brown opined, this stretches the meaning of the term "agreement" beyond all reasonable limits. Slip op. at 7, app. at 20a.

Not only does the majority of the panel stretch the interpretation of the term "agreement" beyond reason, but also, under the majority's interpretation of *D'Oench, Duhme,* virtually no condition not spelled out in a promissory note can defeat the FDIC's right to collect from any borrower from a failed financial institution since *any* common law *or* state *or* federal statutory claim a borrower makes automatically counts as a "secret agreement" not to repay the note. The majority, again relying on *Langley,* 484 U.S. at ____, 108 S. Ct. at 402, makes only one extremely narrow exception to this blanket rule—for "fraud in the factum," narrowly construed. *See* slip op. at 10 n.6, app. at 9a.

What the majority misses is that the entire concept of fraud in the factum—a common law concept complimentary to fraud in the inducement—is alien to securities law. However, as Judge Brown argues, if the claims in this case must be analogized to the common law of contracts in order to be forced into the framework of *D'Oench, Duhme* and *Langley,* the Appellants' federal securities law claims should be analogized to fraud in the factum rather than to fraud in the inducement. As Judge Brown points out,

> Fraud under the Securities Act is significant since it renders the entire instrument void. If void, the FDIC never acquired an interest in the theoretically non-existent "note" in the first place. The [Supreme] Court [in *Langley*] specifically allows the defense of fraud in the factum. Because of its language, § 29 also fits into this narrow exception: "Every contract made in violation . . . *shall be void*". 15 U.S.C. 78cc(b).[6]

Slip op. at 5 (Brown, J., dissenting), app. at 19a.

Judge Brown's reading of the relevant law, unlike the majority's, is straightforward and requires no recasting of Appellants' federal statutory claims as state common law claims and no recasting of the fraudulent sale of securities as a "secret agreement" between the defrauded and the defrauders. However, even if such recasting is undertaken, Judge Brown's analysis demonstrates that Appellants' claims are *not* defeated by *D'Oench, Duhme* and *Langley*. Rather, § 29(b)—on which Petitioners rely and which renders a fraudulent contract for the sale of stock void when necessary for the protection of investors —comports with *Langley's,* holding that fraud in the factum which renders an instrument void defeats the right, title, or interest of the FDIC to an instrument. *See Langley,* 484 U.S. at ____, 108 S. Ct. at 402; slip op. at 5-6, app. at 19a. (Brown, J., dissenting); *see also Olney Savs. & Loan Ass'n v. Trinity Banc Savs. Ass'n.* 885 F.2d 266, 275 (5th Cir. 1989).

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6. The language in § 29(b) has been interpreted as rendering the illegal contract "voidable at the option of the innocent party" so that it may be enforced against the guilty party when it is in the interest of the innocent party to do so; a contract in violation of § 29(b) is, however, interpreted as "void *ab initio*" if that is what is required to protect the innocent investor. *Regional Properties v. Financial and Real Estate Consultants,* 678 F.2d 552, 559 (5th Cir. 1982).

B. The Fifth Circuit Opinion Impermissibly Elevates Federal Common Law Over Federal Securities Law.

In contrast to *Langley,* the FDIC sought collection in the instant case under the federal common law *D'Oench, Duhme* doctrine, not under 12 U.S.C. § 1823(e). Therefore, this case actually involves a conflict between federal common law and federal statutory law, not between two federal statutes. In such circumstances, this Court has repeatedly held that the power of the federal courts to develop federal common law is expressly limited by the actions of Congress. *Texas Indus. Inc. v. Radcliff Materials,* 451 U.S. 630, 640, 101 S. Ct. 2061, 2067 (1981); *City of Milwaukee v. Illinois and Michigan,* 451 U.S. 304, 315 n.8, 101 S. Ct. 1784, 1792 n.8 ("When Congress has spoken its decision controls"). In *Northwest Airlines, Inc. v. Transport Workers Union of America, AFL-CIO,* this Court held:

> federal courts, unlike their state counterparts, are courts of limited jurisdiction that have not been vested with open-ended lawmaking powers . . . . Broadly worded constitutional and statutory provisions necessarily have been given concrete meaning and application by a process of case-by-case judicial decision in the common-law tradition. The Court also recognized a responsibility, in the absence of legislation, to fashion federal common law in cases raising issues of uniquely federal concern, such as the definition of rights or duties of the United States, or the resolution of interstate controversies. However, we consistently have emphasized that the federal lawmaking power is vested in the legislative, not the judicial, branch of government; therefore, federal common law is "subject to the paramount authority of Congress."

451 U.S. 77, 95, 101 S. Ct. 1571, 1582 (1981) (citations omitted). The Court noted:

> A frequently stated principle of statutory construction is that when legislation expressly provides a particular remedy or remedies, courts should not expand the coverage of the statute to subsume other remedies . . . .

451 U.S. 77 at 94 n.30, 101 S. Ct. at 1582 n.30 (citations omitted); *see also Cummingsby Techmeier v. Briggs & Stratton,* 797 F.2d 383, 390 (7th Cir. 1986) ("where Congress has established an extensive regulatory network and expressly announced its intention to occupy the field, federal courts should not create additional rights under the rubric of federal common law").

The federal securities laws constitute a comprehensive remedial scheme designed to protect investors against fraud. *See Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 195, 96 S. Ct. 1375, 1382 (1976). To that end Congress created the Securities Exchange Commission and "provided it with an arsenal of flexible enforcement powers." *Id.* Those powers leave no room for the intrusion of federal common law—especially a provision of common law based on a broad and unspecified "general policy to protect the institution of banking from . . . secret agreements." Nor do the federal securities laws provide failing banks, the FDIC, or the successors to failed banks any immunity from the enforcement of the federal securities laws. In the instant case, therefore, the comprenhensive scheme for the protection of investors set out in the Securities Exchange Act leaves no room for the federal courts to deny investors their statutorily prescribed rights and to grant the FDIC or a successor bank like NCNB additional non-prescribed rights simply because it has

come into possession of a note generated in violation of § 29 of the Act.

Section 29 itself provides the exclusive remedy for violations:

> (b) *Every contract made in violation of any provision of this chapter* or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this chapter or any rule or regulation thereunder, *shall be void* (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) *as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule, or regulation.*
>
> . . . .
>
> (c) *Nothing in this chapter shall be construed . . . (2) to afford a defense to the collection of any debt* or obligation or the enforcement of any lien *by any person who shall have acquired such debt,* obligation, or lien *in good faith for value and without actual knowledge of the violation of* any provision of this chapter or any rule or regulation thereunder affecting the legality of such debt, obligation, or lien.

15 U.S.C. § 78cc (emphasis added). This statute is clear and comprehensive: it voids the rights of anyone who (like the FDIC in this case) acquired an illegal note

with actual knowledge that the note evidenced a transaction in violation of the securities laws,[7] while it protects the rights of anyone (like the FDIC in most other cases) who acquired the illegal note *without* actual knowledge of the facts which made it illegal. In these circumstances, it is contrary to proper legal principles to disregard the comprehensive federal statute covering this issue and to apply court-made federal common law in its place. Similarly, even if § 1823(e) were applicable to this case, it would be improper for the federal courts to decree that § 1823(e)—which is silent about securities fraud—overrides the federal policy protecting investors set out in detail in § 29 of the Securities Exchange Act.

II. THE FIFTH CIRCUIT OPINION CONFLICTS WITH HOLDINGS BY THIS COURT AND BY THE FOURTH, SIXTH, EIGHTH, AND ELEVENTH CIRCUIT COURTS OF APPEAL.

Not only does the preemption of federal securities law claims by the federal common law *D'Oench, Duhme* doctrine violate clear principles of law by subordinating a comprehensive federal statutory scheme to federal common law, but also the Fifth Circuit's holding that *D'Oench, Duhme* trumps the federal securities laws conflicts with prior holdings by this Court and by the Fourth, Sixth,

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7. Because of Petitioners' attempt to intervene in *Bolton,* the FDIC was well aware of Petitioners' fraud claims against RepublicBank well before RepublicBank failed. Indeed, the FDIC was prosecuting virtually identical claims itself. Moreover, NCNB retained RepublicBank's attorneys after its purchase of RepublicBank's assets, and therefore it presumably knew about Appellants' securities fraud suit against RepublicBank before it bought those assets, which included Petitioners' notes. *See supra* at 5-6. Not only would NCNB's due diligence have uncovered *Bolton,* but also in soliciting NCNB's purchase of RepublicBank's assets the FDIC itself would have been guilty of fraud had it not affirmatively disclosed the suit and its allegations to NCNB.

Eighth, and Eleventh Circuit Courts of Appeal. Prior to deciding *D'Oench, Duhme,* this Court expressly held—in a case which it has never overruled—that an insolvent national bank cannot escape liability for misrepresentations made by its officers in selling the bank's own stock; and it has stated that the liability in such cases is the same as if the bank had fraudulently sold other investment securities, the remedy being rescission of the fraudulent stock sales. *Oppenheimer v. Harriman Nat'l Bank & Trust Co. of City of N.Y.*, 301 U.S. 206, 57 S. Ct. 719 (1937).[8]

Like this Court, those circuit courts which have considered securities fraud charges in the failed bank context have continued to apply the securities laws—rather than federal common law—as the rule of decision in those cases. *Gunter v. Hutcheson,* 674 F.2d 862 (11th Cir. 1982), is directly on point and is factually parallel to the present case. In *Gunter* the Eleventh Circuit refused to extend the *D'Oench, Duhme* doctrine to estop the Gunters' federal securities claims. The Gunters had sued former directors and officers of a bank in FDIC receivership seeking rescission of their notes on the basis of the bank's violation of federal and state securities laws. The FDIC moved for summary judgment claiming that *D'Oench, Duhme* estopped the Gunters from bringing their claims. The district court granted summary judgment, and the Eleventh Circuit affirmed but expressly disagreed with the lower court's extension of *D'Oench, Duhme*. The Eleventh Circuit held that, although *D'Oench,*

8. The Fifth Circuit panel majority distinguished *Oppenheimer* on the ground that it says nothing about a federal receiver. Slip op. at 6 n.3, app. at 6a. This distinction, in Petitioners' view, begs the question of whether federal common law overrides federal securities law. *Oppenheimer* clearly says that federal securities law applies to failed banks.

Duhme estopped the Gunters' other causes of action, the strong policies of investor protection embodied in the securities laws prevented *D'Oench, Duhme*'s estoppel of federal securities law claims, stating:

> Although the district court held that a rule of federal common law protecting the FDIC from state and common law fraud claims also prohibited a rescission action for securities law violations, we decline to extend the rule so far. While adopting state law as to the fraud claims would frustrate the federal policies of promoting stability of and confidence in the banking system and thus must give way to a uniform federal rule, we are less confident that these federal policies behind the FDIC Act outweigh the strong policies of investor protection embodied in the securities laws. We need not decide which policies are strongest, however, because we find that the Gunters' securities claims against the FDIC are barred by the defense in § 29(c) of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc(c).

674 F.2d at 874.

The Sixth Circuit also applied federal securities law and not the *D'Oench, Duhme* doctrine to a plaintiff's claims for rescission of a note held by the FDIC in receivership. *Gilman v. Federal Deposit Ins. Corp.*, 660 F.2d 688 (6th Cir. 1981). In *Gilman*, as in *Gunter*, the FDIC won only because it was found to have a complete defense to the plaintiff's rescission claim in that it had acquired the note at issue "in good faith, for value, and *without actual knowledge*" of the fraud as of the day it entered the purchase and assumption and sale of assets agreements. *Id.* at 693-94.[9]

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9. A later Sixth Circuit case, cited by the Fifth Circuit as support for its opinion, *FDIC v. Investors Assocs. X, Ltd.*, 775 F.2d 152,

Again, in a case almost identical to the instant case, the Fourth Circuit applied federal securities law—and not the *D'Oench, Duhme* doctrine. *FDIC v. Aroneck*, 643 F.2d 164 (4th Cir. 1981). In *Aroneck*, the FDIC, in its corporate capacity as successor to American Bank & Trust Co. ("AB&T"), which had failed, sued Aroneck for collection of a note given by Aroneck to AB&T to purchase stock in AB&T's parent corporation. Aroneck denied liability under the federal securities laws. The district court granted summary judgment to the FDIC and the Fourth Circuit affirmed—not because *D'Oench, Duhme* controlled, but because the court found that Aroneck acted *in pari delicto* with AB&T. The only essential differences between *Aroneck* and the instant case, therefore, are the Petitioners did *not* act *in pari delicto* with RepublicBank, and the FDIC *did* have knowledge of Petitioners' fraud claims before RepublicBank failed. Thus the federal securities law defenses that protected the FDIC from Aroneck's counterclaim do not apply.[10]

Finally, at least two of the Circuit Courts have recently held that *D'Oench, Duhme* can be taken too far. Like the Fourth, Sixth, and Eleventh Circuits, the Eighth Circuit

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156 (6th Cir. 1985), mentions in passing that *D'Oench, Duhme* estops a maker of a note held by the FDIC from asserting fraud in the inducement, and state and federal securities law defenses. Significantly, however, *Investors Assocs. X* makes no reference to either *Gunter* or *Gilman*, does not overrule them, and shows no consideration of the issues presented by them.

10. The district courts have also applied federal securities law—and not *D'Oench, Duhme*—to FDIC cases involving federal securities law claims. *See FDIC v. Eagle Properties, Ltd.*, 664 F. Supp. 1027, 1046 (W.D. Tex. 1985) (defendant's federal securities law claims failed because he did not meet his threshold burden of showing the relevant transactions were securities); *FDIC v. Balistreri*, 470 F. Supp. 757 (E.D. Wisc. 1979) (defendant's federal securities law claims failed from failure of proof of fraud).

Court of Appeals has recently held that *D'Oench, Duhme* "affords *no protection* against tort claims against a financial institution," including those arising from "a sale of securities violating Securities and Exchange regulations." *Astrup v. Midwest Fed. Savs. Bank,* 886 F.2d 1057, 1059-60 (8th Cir. 1989) (emphasis added). Similarly, the Eleventh Circuit (the *Gunter* circuit), has recently refused to apply *D'Oench, Duhme* in a federal securities fraud and RICO case brought by shareholders of a failed savings and loan association, Old Freedom. *Vernon v. Resolution Trust Corp.,* 907 F.2d 1101 (11th Cir. 1990). The Court eloquently analyzed the danger of interpreting *D'Oench, Duhme* too broadly, stating,

> New Freedom would have us extend the *D'Oench* doctrine to preserve all assets, whether actually possessed or receivable, acquired by a federal insurer or its successor in interest from all claims tending to diminish those assets, save those claims clearly supported by the records of the insolvent bank.
>
> The expansion of the *D'Oench* doctrine suggested by New Freedom might well further the background goal of favoring and facilitating the purchase and assumption of insolvent banks over liquidation. We decline to adopt such a rule, however, as we believe it would be both inappropriate and unnecessary in this appeal.
>
> . . .
>
> Certain claims, such as tort claims, might not appear in the books of a failed bank and yet easily be shown to be valid. The rule proposed by New Freedom would bar such claims from being successfully asserted when Congress has provided that such claims be paid. New Freedom's rule cannot prevail.

Id. at 1108. The Fifth Circuit thus stands alone in proclaiming that federal securities law claims and defenses are swept aside by *D'Oench, Duhme,* even as the other circuits which have considered the question have held to the contrary, recognizing the danger of too facile an application of the *D'Oench, Duhme* doctrine.

III. THE ERRONEOUS PRECLUSION OF FEDERAL SECURITIES LAW CLAIMS BY *D'OENCH, DUHME* GRANTS A WINDFALL TO THE SUCCESSORS TO FAILED FINANCIAL INSTITUTIONS AND ENCOURAGES FRAUD.

Having miscast Petitioners' securities fraud claims as a villainous "secret agreement" not to repay funds which properly belong to the FDIC, rather than as securities fraud claims well known to the FDIC before Republic-Bank failed, which in fact they were, the Fifth Circuit panel majority in the instant case justified its holding on the ground that "[n]o authority suggests a right to be compensated by the federal government because one's investments fail." Slip op. at 14, app. at 13a. The majority then observed that "precluding this action does not deprive the Plaintiffs of protection under the federal securities laws" since they could sue the individuals who defrauded them. Slip op. at 14, app. at 13a. The panel went on to note, "As a matter of equity we see no reason the Plaintiffs should be in a better position simply because the institutions that defrauded them happened to fail rather than survive." Slip op. at 14 n.7, app. at 13a.

In this case, the Fifth Circuit panel majority exactly misconstrued the effect of their holding on Petitioners: depriving them of their right to sue the institution which

defrauded them places them in a *worse* position than they would otherwise be in, simply because the institution that fraudulently sold them stock happened to be not a brokerage house or an individual but a bank—and a bank that failed rather than survived. Appellants instituted this suit well before RepublicBank failed. Had RepublicBank *not* failed, Petitioners' suit would, of necessity, have been heard on its merits, and Petitioners'—if their securities fraud claims were sound—would have had redress in the form of rescission of their contracts or damages against RepublicBank. Under the law established by the Fifth Circuit panel, however, RepublicBank and its successor NCNB were both relieved of the necessity to defend this suit on its merits by the failure of RepublicBank and were enabled to collect on assets which otherwise they could not have counted as good.

Under the Fifth Circuit's interpretation of the law, in a situation like the present one *both* the FDIC and the successor institution get a windfall: they are both enabled to recover on assets which they knew when the institution failed and was sold were already the subject of federal securities fraud litigation.[11] Even more significantly, a foundering financial institution is encouraged to engage in securities fraud, knowing that even if its fraudulent acitvities are discovered and the whistle is blown on those activities, it will be absolved of all evil in receivership while its victims pay the price. Conversely, potential complainants who are defrauded under a stock purchase scheme involving a failing bank are told that since they

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11. Indeed, this case is particularly egregious because here the FDIC as receiver for TNB-Westheimer was asserting virtually identical securities fraud claims to those asserted by Petitioners at the moment RepublicBank failed and the FDIC took over as receiver there. *See* slip op. at 3, app. at 3a.

guessed wrong and the institution against which they brought their suit failed, their suit against that institution is barred by *D'Oench, Duhme.* It is unfortunate that plaintiffs who also guess wrong and fail to include in their suit bank officers or employees may find their claims barred by limitations by the time the institution fails.

In other words, the Fifth Circuit opinion places persons with securities claims against a financial institution that happens to fail in a markedly worse position than if the institution had survived and places the failed institution, its officers and directors, and any successor institution all in a markedly better position than if the institution had survived. The decision also places investors who deal with weak banks in a dramtically worse position than other investors. This is an invitation to securities fraud on a grand scale by weak and foundering financial institutions. Ironically, by contrast, properly applying federal securities law in cases such as this does not open the floodgates to litigation, since only valid federal securities law claims can survive the bank's failure. *See* cases cited *supra,* in which the FDIC prevailed under the securities laws themselves. The only effect of a proper interpretation of the law—which would not have *D'Oench, Duhme* override federal securities law—is to preserve valid federal statutory claims. Persons with weak or invalid federal claims have nothing to gain by bringing them.

As cited by the Fifth Circuit panel majority itself, the *D'Oench, Duhme* doctrine has two purposes:

> One purpose . . . is to allow federal and state bank examiners to rely on a bank's records in evaluating the worth of the bank's assets . . . . A second purpose . . . [is to] ensure mature consideration of

> unusual loan transactions by senior bank officials, and prevent fraudulent insertion of new terms, with the collusion of bank employees, when a bank appears headed for failure.

Slip op. at 8, app. at 8a (quoting *Langley*, 486 U.S. at 91-92, 108 S. Ct. at 401). As applied by the panel, however, the *D'Oench, Duhme* doctrine has precisely the opposite effect: it allows bank examiners to ignore outstanding federal claims against failed financial institutions and therefore to assign a *greater* value to the institution's assets than appears on the institution's own records; and it encourages fraudulent securities transactions with the collusion of bank employees when a bank appears headed for failure.

As Judge Brown made clear in his dissent, and as all the federal Circuit Courts which have refused to extend *D'Oench, Duhme* to federal securities law claims have implicitly or explicitly recognized, this case involves a balancing between the generalized public purpose of *D'Oench, Duhme*—which is to protect the public treasury—and the specialized public purpose of the Securities Exchange Act of 1934—which is to punish and thereby prevent fraud in the sale of securities in the public markets. *See* slip op. at 11 (Brown, J., dissenting), app. at 24a. The more particularized public policy underlying the securities laws expressly provides for situations like the present one, whereas the generalized purpose of protecting the public purse does not. In these circumstances, the federal securities laws, and not the federal common law, should control.

CONCLUSION

The Fifth Circuit's holding in the instant case that the federal common law *D'Oench, Duhme* doctrine shields the FDIC and the successor to a failed financial institution from federal securities law claims and defenses (1) impermissibly gives federal common law priority over the federal securities laws promulgated by Congress, (2) conflicts with the prior stance of this Court that failed banks are not immune from federal securities fraud claims, (3) conflicts with holdings by the Fourth, Sixth, Eighth, and Eleventh Circuit Courts of Appeal, and (4) encourages fraud.

WHEREFORE, for the foregoing reasons, Petitioners Rogers and Singletary pray that the Court grant their petition for writ of certiorari to the Fifth Circuit Court of Appeals.

Respectfully submitted

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APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 89-2963

WADE A. KILPATRICK, ET AL.,
Plaintiffs,

STAN E. GOLUB, ET AL.,
Plaintiffs-Appellants,

versus

JOHN C. RIDDLE, ET AL.,
Defendants,

THE FEDERAL DEPOSIT INSURANCE CORP.,
as Receiver for FIRST REPUBLICBANK
HOUSTON, N.A., ET AL.,
Defendants-Appellees.

Appeal from the United States District Court for the
Southern District of Texas

(July 25, 1990)

Before BROWN, JOLLY and DAVIS, Circuit Judges.

E. GRADY JOLLY, Circuit Judge:

This case presents the following question: Does the *D'Oench, Duhme* doctrine,[1] which protects the Federal Deposit Insurance Corporation from the effect of unrecorded agreements between an insured bank and its customers, preclude borrowers who were defrauded by failed banks, from bringing an action under federal securities laws against the FDIC as receiver? Although several circuits have touched on this question, none have squarely considered it. Supreme Court precedent, however, now makes clear that debtors may not raise bank fraud as a defense to the FDIC's collection efforts. The *D'Oench, Duhme* doctrine would be effectively nullified if borrowers could characterize their fraud-based defenses as independent causes of action and maintain them against the federal receiver. Thus, although the plaintiffs may, of course, pursue actions for securities fraud against the individuals involved, we conclude that they may not recast their barred defenses as causes of action under the federal securities laws.

I

This case arises from a summary judgment granted defendants, the FDIC, and NCNB, the bridge bank used to rescue the failed institutions in this case. The plaintiffs are investors who executed promissory notes in favor of First RepublicBank ("FRB"), the failed bank. When FRB failed, these notes were acquired by the FDIC in its capacity as receiver. The FDIC then assigned the plaintiffs' notes to the bridge bank. The plaintiffs originally sued FRB for alleged fraud in the promotion and sale of

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1. The doctrine was originally stated in *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 62 S.Ct. 676 (1942), and was later codified at 12 U.S.C. § 1823(e).

certain bank stock, which FRB underwrote by inducing the plaintiffs to execute the promissory notes at issue. The plaintiffs then added the defendants FDIC and NCNB, as successors-in-interest.

This litigation has a complex procedural history that is not relevant to the issue on appeal. As this case appears before us, the plaintiffs seek rescission of these notes on the ground that they are invalid because they were originally obtained through fraud. They allege that FRB assisted two men, who were heavily in debt to it, in a scheme to defraud investors. The two alleged swindlers promoted a plan to open several branches of the Texas National Bank (TNB). FRB financed the plan by loaning the investors money for the purchase of new TNB stock. The investors executed promissory notes and FRB thus acquired new collateral for the debts owed it by the alleged swindlers.

The plaintiffs allege fraud in that FRB never told them that the TNB stock was subject to a voting trust, which gave control over the stock to the two alleged swindlers. Furthermore, the plaintiffs allege that the stock was overvalued, and that the new banks were doomed to fail from the outset, and that this was all known by FRB. In the end, however, the net result of the stock-for-promissory note transactions was to give FRB fresh obligations from creditworthy investors by simply loaning money for a very short time in paper transactions that were essentially riskless to FRB. Although it was FRB that is alleged to have committed the fraud, the plaintiffs contend that the FDIC had acquired knowledge of FRB's fraud by the time it became receiver, because it had previously participated in litigation involving the failed TNB branches. Since the FDIC knew of FRB's fraud,

and informed NCNB of it, neither the FDIC nor NCNB can escape FRB's liability as "innocent purchasers" of the notes.

The plaintiffs seek recovery from the FDIC and NCNB on eight bases, all of which involve alleged misrepresentation or fraud on the part of the alleged swindlers and FRB. Among these causes of action are claims under federal and state securities laws.[2] They assert that the FDIC was liable for FRB's fraudulent actions, and thus cannot collect on the notes, because it acquired them with actual knowledge of the fraud gained from its participation in the TNB litigation. NCNB, as assignee of FDIC, can have no greater right to collect on them than did the FDIC. NCNB counterclaimed to enforce the notes.

The defendants rely on the *D'Oench, Duhme* doctrine in two ways: they argue that it is a complete defense to the investors' fraud claims and that it bars their defenses against enforcement of the notes. The district court granted summary judgment to the defendants. It concluded that the federal common law *D'Oench, Duhme* doctrine, which precludes defenses to recovery against a closed bank that are premised on undisclosed agreements between the borrower and the bank, both barred the plaintiffs' claims and allowed the defendants' counterclaims. Plaintiffs filed a timely notice of appeal.

II

The plaintiffs raise three arguments. First, although

2. Their claims are based on section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5, section 33 of the Texas Securities Act, civil conspiracy, statutory and common law fraud, breach of the duty of good faith and fair dealing, and violations of section 29 of the Securities Exchange Act of 1934 and section 12(2) of the Securities Act of 1933.

they concede that the *D'Oench, Duhme* doctrine precludes many of their claims, they contend that it cannot bar their actions under the federal securities laws. Second, they argue that the FDIC and NCNB cannot escape liability for securities violations as "innocent purchasers" under section 29 of the Securities Exchange Act, because they took the notes with actual knowledge of the plaintiffs' claims and defenses. Finally, they argue that summary judgment was inappropriate because genuine issues of material fact remain concerning misrepresentations made by FRB in the issuance of the securities. Our resolution of the first issue is dispositive of the entire appeal.

III

The essence of the plaintiffs' argument is that the *D'Oench, Duhme* doctrine cannot bar their federal securities law claims, because this result would empower the FDIC to enforce agreements that are illegal under federal securities laws. They contend that the Supreme Court has held insolvent national banks liable for misrepresentations made in the sale of their own stock,[3] and that this court has not held that the *D'Oench, Duhme* doctrine trumps federal securities law. They further argue that, as a policy matter, protecting investors by holding the FDIC liable for securities fraud on the part of failed banks need not undercut the system of national bank regulation. They assert that the FDIC's liability may

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3. *Oppenheimer v. Harriman Nat'l Bank & Trust Co. of City of N.Y.*, 301 U.S. 206, 57 S.Ct. 719 (1937). *Oppenheimer*, decided several years before *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 62 S.Ct. 676 (1942), simply holds that bank stockholders defrauded into purchasing bank stock have the same priority after the bank fails as other unsecured creditors. It says nothing about their ability to recover from a federal receiver.

appropriately be limited to cases in which it assumes a failed bank's liabilities with actual knowledge of the bank's fraudulent securities dealings. Given the FDIC's participation in the TNB litigation, the plaintiffs argue that the FDIC had knowledge of the fraud behind this transaction before it acquired FRB and consequently was not an "innocent purchaser" of the notes in question.

Although the plaintiffs are correct that only one court has explicitly held that federal securities claims may be barred by the *D'Oench, Duhme* doctrine, recent Supreme Court precedent makes clear that claims that are in essence indistinguishable from those the plaintiffs seek to maintain are barred by the doctrine. Moreover, several courts have held that the doctrine bars *state* securities fraud claims, which often provide causes of action that overlap the federal securities laws. Finally, and most importantly, permitting borrowers to maintain federal securities claims would enable them to simply recast as affirmative causes of action the very defenses that the Supreme Court has long held are precluded by the doctrine.

A

The *D'Oench, Duhme* doctrine, as originally stated, holds that when a federally insured bank fails, borrowers from the bank may not later defend against collection efforts of a federal receiver by arguing that they had an unrecorded agreement with the bank. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 459-60, 62 S.Ct. 676, 680 (1942). In *D'Oench*, the borrower had executed obligations to an insured institution but claimed, after the bank failed, that the bank had orally agreed that these obligations would not be enforced. This oral side arrangement became the paradigmatic "secret agreement" barred by

the doctrine. Congress has embodied this common law doctrine in statute.[4] As codified, the doctrine precludes borrowers from avoiding obligations to failed banks unless they have an arrangement in writing, that was executed by the bank and the borrower, approved by the bank's board and listed in the bank's records.[5]

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4. There are two *D'Oench, Duhme* doctrines, one statutory (12 U.S.C. § 1823(e)) and one of common law. Until recently, only the common law version protected the FDIC when it acted in its capacity as receiver. See *Beighley v. FDIC*, 868 F.2d 776, 783 ("Section 1823(e) is not available as a bar to claims of defenses against the FDIC when it is acting in its capacity as receiver"). On August 9, 1989 Congress amended the statutory version, making it available to the FDIC-Receiver. 12 U.S.C. § 1823(e). This action was brought before section 1823(e) was amended, and involves the FDIC in its capacity as receiver. We need not consider, however, whether this change applies to this case, because we have long held that both doctrines bar similar defenses by borrowers. *See Beighley v. FDIC*, 868 F.2d 776, 784 (5th Cir. 1989) (noting that "[c]ourts often consider the [common law] *D'Oench, Duhme* doctrine and § 1823(e) in tandem, looking to the common law when construing the statute") and cases cited therein; *Olney Sav. & Loan Ass'n v. Trinity Banc Sav. Ass'n*, 885 F.2d 266, 274 (5th Cir. 1989) ("[a]s the aims of § 1823(e) and *D'Oench* are identical and § 1823(e) is a codification of *D'Oench* and its progeny, the reasoning applied in § 1823(e) cases is applicable to *D'Oench cases*"). *See also FDIC v. Condit*, 861 F.2d 853, 858, n.5 (5th Cir. 1988).

5. 12 U.S.C. § 1823(e) provides:

(e) Agreements against interests of Corporation

No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this section or section 1821 of this title, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—

(1) is in writing,

(2) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution,

(3) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and

(4) has been, continuously, from the time of its execution, an official record of the depository institution.

As the Supreme Court has recently explained, the doctrine has two purposes.

> One purpose . . . is to allow federal and state bank examiners to rely on a bank's records in evaluating the worth of the bank's assets . . . . A second purpose . . . [is to] ensure mature consideration of unusual loan transactions by senior bank officials, and prevent fraudulent insertion of new terms, with the collusion of bank employees, when a bank appears headed for failure.

Langley v. FDIC, 484 U.S. 86, 91-92, 108 S.Ct. 396, 401 (1987). Since the initial statement of the doctrine in *D'Oench, Duhme,* the Court has expanded its preclusive effect well beyond the context of an oral "secret agreement" between the bank and the borrower. Most recently, in *Langley* the Supreme Court extended the doctrine to preclude the same defense that the plaintiffs seek to advance here: that the obligation to the failed bank was procured through fraud in the inducement.

In *Langley,* the Langleys borrowed money from a bank in order to buy land, and executed a mortgage as security for the loan. After the bank failed the Langleys sued it, claiming that the bank had deceived them concerning the land's value. They alleged that the bank had represented the land as larger and more valuable than it in fact was. None of these representations were recorded in any of the loan documents.

As recevier, the FDIC acquired the Langleys' mortgage among the bank's assets and sought to enforce it. The Langleys claimed that the mortgage was unenforceable because it had been predicated on fraud. They argued that the statute bars only defenses based on an unrecorded

"agreement," and an agreement obviously requires mutual consent. Their defense, by contrast, alleged an unrecorded misrepresentation by the defrauding bank. Unilateral misrepresentation, their argument urged, is not an "agreement," and thus is not barred by the *D'Oench, Duhme* doctrine.

The Court rejected the Langleys' argument and held that agreements invalidated by section 1823(e) include "agreements" predicated on fraud, noting that *D'Oench, Duhme* itself applied whenever the maker "lent himself to a scheme or arrangement whereby the banking authority . . . was likely to be misled." 315 U.S. at 460. Unwritten representations concerning the actual size of the land or the value of the mineral deposits would naturally mislead an outside examiner, simply because they were unwritten. "Certainly, one who signs a facially unqualified note subject to an unwritten and unrecorded condition upon its repayment has lent himself to a scheme or arrangement that is likely to mislead the banking authority, whether the condition consists of performance of a counter-promise (as in *D'Oench, Duhme*) *or of the truthfulness of a warranted fact.*" 484 U.S. at 93, 108 S.Ct. at 402 (emphasis added).[6] Thus, it is now clear that borrowers who execute facially unqualified obliga-

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6. The Supreme Court did identify one exception to the broad reach of section 1823(e) but it is inapplicable in this case. Where the bank engages in fraud "in the *factum*" rather than fraud in the inducement, there is no valid obligation on the part of the borrower under the principle that fraud vitiates consent. The borrowers here knowingly executed promissory notes in favor of FRB. They claim that they did not realize the risk of the venture because of the disguised voting trust, the heavy indebtedness of the promoters, and the inflated value of the TNB stock. These are allegations of fraud in the inducement. The plaintiffs' obligations to the bank, and thus to NCNB, would therefore be voidable rather than void.

tions may not prevent a federal receiver's collection efforts by claiming that they were induced to execute the obligations by fraud.

B

As we have noted, the plaintiffs have alleged that they were fraudulently induced to execute promissory notes. The notes were part of a scheme in which they were induced to purchase worthless stock with the loan proceeds. Viewing the facts and inferences in the light most favorable to the nonmovants, we presume, without deciding, that the plaintiffs have stated a claim for securities fraud against the promoters and FRB. *Barrett v. Computers Servs., Inc.*, 884 F.2d 214, 215 (5th Cir. 1989). We also observe at the outset that if the *D'Oench, Duhme* doctrine protects the FDIC, it also protects NCNB, because "we recently extended *D'Oench, Duhme* to *'assignees* of the FDIC.' " *Porras v. Petroplex Sav. Ass'n*, 903 F.2d 379, ____ (5th Cir. 1990) slip op. pp. 4414, 4416 (citing *Bell & Murphy & Assocs. v. Interfirst Bank Gateway*, 894 F.2d 750, 754-55 (5th Cir. 1990)).

It is further clear that if the plaintiffs' defenses are barred by the *D'Oench, Duhme* doctrine, then their defenses framed as causes of action must also be barred, because any other result would nullify the doctrine. *Bell & Murphy & Assocs. v. Interfirst Bank Gateway*, 894 F.2d 750, 753 (5th Cir. 1990) ("this argument [is] meritless in light of our recent holding in *Beighley* that the *D'Oench, Duhme* rule bars affirmative claims based upon unrecorded agreements"). Furthermore, prior knowledge of FRB's alleged fraud that the FDIC may have gained from the TNB litigation will not aid the plaintiffs' defense, because "even if the FDIC had knowledge of the oral

misrepresentation prior to its acquisition of the note[s], such knowledge is not relevant to whether § 1823(e) applies. The voidable interest is transferable whether or not FDIC knows of the misrepresentation or fraud which produces the voidability." *FDIC v. Kratz,* 898 F.2d 669, 671 (8th Cir. 1990) (citing *Langley*). *See also FDIC v. Roldan Fonseca,* 795 F.2d 1102, 1107 (1st Cir. 1986) (claim of knowledge is "precisely what FDIC is protected from by virtue of Section 1823(e)"). The question then is this: may the plaintiffs distinguish themselves from all the previously cited authority, and defend against the collection efforts of the federal receiver on the ground that the "agreement" violated federal securities laws? In a word, no.

It seems clear to us that under the rule of *Langley* and the principles underlying the *D'Oench, Duhme* doctrine, the plaintiffs' claims and defenses must be barred. We think that *Langley v. FDIC* refutes the plaintiffs' arguments since it barred a borrower's defense that is essentially indistinguishable from the plaintiffs' claims in this case. "Following *Langley,* we have held that misrepresentations to borrowers cannot be asserted as a defense to recovery by the FSLIC on facially unqualified loan documents." *McLemore v. Landry,* 898 F.2d 996, 1002 (5th Cir. 1990). As in *Langley,* the borrowers here argue that certain warranted facts concerning their loans, namely the value of the underlying asset securing their promissory notes, were misrepresented to them by the bank. Except for the fact that the asset in this case is stock rather than land, and its sale thus regulated by federal law, the cases are the same.

It is true that only one court has expressly rejected federal securities law defenses on the basis of the *D'Oench,*

Duhme doctrine. In *FDIC v. Investors Associates X, Ltd.*, 775 F.2d 152, 156 (6th Cir. 1985), the court rejected arguments of "fraud in the inducement, and state and federal securities law defenses" asserted against the FDIC. *But see Gilman v. FDIC,* 660 F.2d 688, 693-94 (6th Cir. 1981) (suggesting possible right of borrowers to rescind obligations made in violation of securities laws), and *Gunter v. Hutcheson,* 674 F.2d 862, 874 (11th Cir. 1982) (identifying but not deciding question). These decisions were all rendered before the Supreme Court's decision in *Langley.* Although no Fifth Circuit case has expressly extended the *D'Oench, Duhme* doctrine to bar claims arising under the federal securities laws, this court has held (after *Langley* was decided) that a plaintiff cannot assert similar state common law claims of fraud, breach of contract, or breach of fiduciary duty against an FDIC receiver. *Beighley v. FDIC,* 868 F.2d 776, 784, n.12 (5th Cir. 1989).

We find the fact that the "agreement" in this case allegedly involved securities fraud is unimportant for purposes of *D'Oench, Duhme* analysis. It is not the nature or enforceability of an agreement between a bank and borrower that controls the application of the *D'Oench, Duhme* doctrine; if the agreement is unwritten, *D'Oench, Duhme* applies. *D'Oench,* 315 U.S. at 459, 62 S.Ct. at 680. *See also* 12 U.S.C. § 1823(e). The plaintiffs contend, nevertheless, that a "balancing of federal policies . . . demands that investor protection embodied in the securities laws outweigh the federal policies behind the *D'Oench, Duhme* doctrine." We do not see that this case requires striking such a balance.

First, as we have noted earlier, precluding this action does not deprive the plaintiffs of protection under the

federal securities laws. They may sue the individuals who actually defrauded them. Application of the doctrine here only denies a certain remedy, namely, rescission of voluntarily undertaken obligations to the federally insured bank. Second, no authority suggests a right to be compensated by the federal government because one's investments fail. Although there is no federal policy of protecting investors by the government underwriting privately issued securities,[7] *Huddleston v. Herman & MacLean,* 604 F.2d 534, 549 (5th Cir. 1981) there is a federal policy of protecting federally insured banks from the effect of unrecorded agreements. Obviously, *D'Oench, Duhme* is not designed to protect investors. The "doctrine thus favors the interests of depositors and creditors of a failed bank, who cannot protect themselves from secret agreements, over the interests of borrowers, who can." *Campbell Leasing, Inc. v. FDIC,* 901 F.2d 1244, 1248 (5th Cir. 1990).

Finally, this result is not only consistent with recent precedent concerning the scope of the *D'Oench, Duhme* doctrine, but also reaffirms a basic principle underlying that doctrine, which is of particular relevance today. It is the "federal policy to protect [the FDIC] *and the public funds which it administers* against misrepresentations as to the securities or other assets in the portfolios of the banks which [it] insures or to which it makes loans." *D'Oench, Duhme & Co. v. FDIC,* 315 U.S. 447, 457, 62 S.Ct. 676, 679 (1942). This policy is undermined

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7. As a matter of equity, we see no reason the plaintiffs should be in a better position simply because the institutions that defrauded them happened to fail rather than survive. We reiterate that barring their suit against the federal receiver does not preclude their suing the individuals who actually defrauded them.

just as much by unrecorded representations regarding securities as by secret agreements that condition the enforceability of obligations to a federally insured bank. We must therefore conclude that claims under the federal securities laws provide no basis from which to carve an exception from the *D'Oench, Duhme* doctrine.

IV

Because we conclude that the *D'Oench, Duhme* doctrine bars the plaintiffs' claims and defenses even if FRB committed fraud of which the FDIC had knowledge, we need not consider whether the defendants are "innocent purchasers" or whether there were genuine issues of material fact concerning the alleged fraud.

For the foregoing reasons, the judgment of the district court is

AFFIRMED.

JOHN R. BROWN, Circuit Judge, dissenting.

I must dissent with the Court's main holding in this case. The question is whether the *D'Oench, Duhme* doctrine[1] and it's so-called codified counter-part,[2] 12 U.S.C. § 1823(e),[3] estop all defenses to the repayment of loans of failed banks which the FDIC has assumed in receivership. Is the doctrine so powerful and all en-

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1. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 62 S.Ct. 676, 86 L.Ed. 956 (1942).

2. The often recited statement that § 1823(e) is a codification of *D'Oench, Duhme* does not bear analysis. The specific requirements of § 1823(e) are in no way provided, or even mentioned, in *D'Oench, Duhme.*

The requirement that the agreement of non-liability be in writing and approved by the bank board of directors and contained in the permanent records (see items 1-4 of § 1823(e)) are not the work of the Supreme Court as reflected in this much cited opinion. These are exclusively the work of Congress.

The distinction is more than rhetorical. The test established in *D'Oench, Duhme* is "whether the note was designed to deceive the creditors or the public authority, or would tend to have that effect." *D'Oench, Duhme*, 315 U.S. at 460, 62 S.Ct. at ___, 86 L.Ed. at ___. If 1823(e) does not apply (see Majority Opinion, *supra* note 4.), a failure to comply specifically with the requirements of 1823(e) will not be prima facie evidence of the applicability of *D'Oench, Duhme.*

3. 12 U.S.C. § 1823(e):

> No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this action, either as security for a loan or by purchase, shall be valid against the corporation unless such an agreement
>
> (1) shall be in writing,
>
> (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the bank,
>
> (3) shall have been approved by the board of directors of the bank or it's loan committee, which approval shall be reflected in the minutes of said board or committee, and
>
> (4) shall have been, continuously, from the time of it's execution, an official record of the bank.

compassing that nothing can stand in its way, including federal statutes protecting investors? In my judgment, the answer has to be no. There is a limit to the protection needed by the FDIC.

I.

I do concur with the Court on several points. It is well established that when the *D'Oench, Duhme* doctrine applies, 1) the debtor will not be allowed to frame his defenses as an affirmative cause of action, and 2) bridge banks will be afforded the same protection as the FDIC.[4] I also agree that the evidence must be looked at in the light most favorable to the non-movants (investors) and assume, as does the Court for purposes of summary judgment, that they have stated a question of fact about the securities fraud against the promoters and FRB.

The FDIC asserts that the *D'Oench, Duhme* doctrine estops the appellants-investors from using an affirmative claim of fraud in the sale of securities to negate the obligation on certain notes and guarantees. The fraud claim is based on the Securities Exchange Act of 1934, § 29.[5] The appellants claim that FRB violated the Securi-

4. *Bell & Murphy & Assocs. v. Interfirst Bank Gateway*, 894 F.2d 750, 754-55 (5th Cir. 1990); *Porras v. Petroplex Savings Assoc.*, No. 89-1796, slip op. at 4414 (1990).

5. § 29 as codified by 15 U.S.C. § 78cc:

> (b) Every contract made in violation of any provision of this chapter or any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of any provision of this chapter or any rule or regulation thereunder, *shall be void* (1) as regards the rights of any person who, in violation of any such provision, rule or regulation, shall have made or engaged in the performance of

ties Act in several ways. 1) Although the bank knew that Riddles and Suttles were millions of dollars in debt they continued to promote the sale of stock; 2) the bank failed to disclose the actual precarious financial position of TNB when they promoted the sale of stock; and 3) the bank did not reveal the nature of the voting stock.[6]

The implication of the FDIC's position is an unacceptable expansion of both the common law and § 1823(e).

Until today, this Circuit has not ruled on whether *D'Oench, Duhme* should preclude fraud defenses based on federal securities law. However, the 11th Circuit dealt with the issue in *Gunter v. Hutcheson,* 674 F.2d 862 (11th Cir. 1982), *cert. denied,* 459 U.S. 826, 103 S.Ct. 68 (1982). "We are less confident that these Federal policies behind the FDIC act [*D'Oench, Duhme* doctrine] outweigh the strong policies of investor protection embodied in securities law." *Gunter,* 674 F.2d at 874.

In light of the current savings and loans' crisis which may cost taxpayers up to $500 billion, President Franklin Roosevelt's letter to the 73rd Congress, urging the passage of the Security Act of 1933[7] continues to reflect strong congressional policy: "What we seek is the return to a

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any such contract and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule or regulation: 15 U.S.C. § 78cc (italics added).

6. In their original complaint, the plaintiffs alleged that FRB violated 15 U.S.C. § 78j(b), 17 C.F.R. § 240.10b-5, and 15 U.S.C. § 78t.

7. The Security Act of 1933 preceded the Security Exchange Act of 1934. The 1934 Act was a continuation of the policies which were enacted in 1933.

clearer understanding of the ancient truth that those who manage banks, corporations, and other agencies handling or using other people's money are trustees acting for others."[8] The policy of fiduciary responsibility and good faith securities dealing should not be summarily overridden by the policy of assuring full information to bank regulators as reflected in the *D'Oench, Duhme* doctrine.

The Securities Exchange Act is different from state and common law fraud claims for several reasons: 1) Unlike state and common law fraud claims, the Act makes the transaction *void,* not merely voidable; 2) the necessity for uniform adjudication of a peculiarly federal problem is satisfied because the Act is a federal statute; and 3) the statute also provides the FDIC protection from most actions under the Securities Act since actual participation or knowledge of the fraudulent transaction on the part of the FDIC is required.[9]

In *Langley v. FDIC,* 484 U.S. 86, 108 S.Ct. 396, 98 L.Ed.2d 340 (1987), the Supreme Court held that fraud in the inducement by the lending bank was precluded

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8. H.R. Report No. 85, 73rd Cong. 1st sess., _____ (1933).

9. The pertinent section provides:
(c) Nothing in this chapter shall be construed (1) to affect the validity of a loan or extension of credit . . . unless at the time of making the loan or extension of credit . . . the person making such loan or extension of credit . . . or *acquiring such lien shall have actual knowledge* of facts by reason of which the making of such a loan or extension of credit . . . or the acquisition of such lien is a violation of the provisions of this chapter or any rule or regulation thereunder, or (2) to afford a defense to the collection of any debt or obligation or the enforcement of any lien by any person who shall have acquired such debt, obligation, or lien in good faith for value and *without actual knowledge of the violation of any provision of this chapter* or any rule or regulation thereunder affecting the legality of such debt, obligation, or lien. 15 U.S.C. § 78cc(c) (italics added).

by *D'Oench, Duhme* and 1823(e). However, the Court pointed out that the doctrine will not always apply: "The presence of fraud could be relevant, however, to another requirement of § 1823(e), namely the requirement that the agreement in question 'tend . . . to diminish or defeat the right, title or interest' of the FDIC." *Langley* 484 U.S. at ____, 108 S.Ct. at 402, 98 L.Ed.2d at ____. *Olney Sav. & Loan Ass'n v. Trinity Banc Sav. Ass'n,* 885 F.2d 266, 275 (5th Cir. 1989).

Fraud under the Securities Act is significant since it renders the entire instrument void. If void, the FDIC never acquired an interest in the theoretically non-existent "note" in the first place. The Court specifically allows the defense of fraud in the factum. Because of its language, § 29 also fits into this narrow exception: "Every contract made in violation . . . *shall be void.*" 15 U.S.C. 78cc(b).

The FDIC argues that void should be read as voidable and cites *Gunter.* The Court also states that because the fraud is merely fraud in the inducement, the contract is merely voidable. However, the 11th Circuit in *Gunter* said that "void" could be read only as "voidable" "to assure that the party who has violated the securities laws cannot escape liability . . . no countervailing reasons exist to limit the express protection afforded innocent purchasers of debt securities by § 29." *Gunter,* 674 F.2d at 876. The 5th Circuit also dealt with the construction of § 29. In *Regional Properties v. Financial Real Estate Consulting Co.,* 678 F.2d 552 (5th Cir. 1982) this Court pronounced that it's earlier position that § 29 made the contract "void ab initio"[10] should be changed to the extent

10. *Eastside Church of Christ v. National Plan, Inc.,* 391 F.2d 357, 363 (5th Cir.), *cert. denied,* 393 U.S. 913, 89 S.Ct. 234, 240, 21 L.Ed.2d 198 (1968).

that violators of the act could not use the "void" language to rescind a contract to the detriment of an innocent party.[11] Because there is, in this case, no reason to read "void" as "voidable" to protect the innocent purchaser the Court is left with the statute as written.

Section 1823(e) protects FDIC from "agreements which tend to diminish or defeat the interest of the Corporation in any asset acquired by it . . . ."[12] This will protect the FDIC in the majority of cases. It will not be successful when 1) the debtor is able to meet the four requirements of § 1823(e), or 2) there is no actual agreement at all.

Naturally I accept the Supreme Court's broad definition of agreement. "As used in commercial and contract law, the term 'agreement' often has 'a wider meaning than promise . . . and embraces such a condition on performance.' " *Langley*, 484 U.S. at ____, 108 S.Ct. at 401, 98 L.Ed.2d at ____. The conditions precedent to the performance are also part of the agreement. FDIC contends that the statutory requirement that the FRB not act fraudulently in the sale of stock is a condition to repayment. Because the investors did not write down that FRB was not to defraud them, the investors cannot rescind the fraudulent contracts. This is stretching the intent of the doctrine beyond reasonable limits.

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11. The Supreme Court also dealt with this issue in *Mills v. Electric Auto-Lite*, 396 U.S. 375, 90 S.Ct. 616, 24 L.Ed.2d 593 (1969). The Court also said that "void" should be read as "voidable" to protect the rights of the innocent party. However, they point out that because the statute uses the "void" language "establishes that the guilty party is precluded from enforcing the contract against the unwilling innocent party." *Mills*, 396 U.S. at 386, 90 S.Ct. at __, 24 L.Ed. at __. The concern of the Court is to protect the innocent party. In this case, the innocent, unwilling, party is better served by reading the language as "void".

12. 12 U.S.C. 1823(e).

The Court sees no difference between the situation in *Langley* and the facts in the present case. In *Langley,* the misrepresentation made by the lending bank was the amount of land and mineral rights actually involved in the transaction. Although one might seriously doubt that a bank would record permanently that it made such misrepresentations, theoretically at least, the borrowers could have made the bank document the actual amounts of land and mineral rights in the bank records or in the minutes of bank officer meetings. However, the fact that FRB, Riddles, and Suttles were defrauding the innocent investors (borrowers) was not a thing likely to be recorded in the banks permanent records as "smoking gun" proof of its fraudulent intent.

The issue is not that the worth of the stocks was not recorded. Investors do not base their claim on an oral agreement as to the worth of the stocks. Rather, their claim is that the *sale* of stock was fraudulent. When FRB failed to disclose what it knew about the precarious financial situation of TNB and still encouraged and financed the stock sales, it was an active participant in defrauding the investors.

To require the defrauded investors to somehow show in the bank records—which are normally highly confidential records available to no outsiders—that they had been defrauded would be to require unlikely conduct that would add the burden of "let the borrower beware" to "let the buyer beware" unless the borrower could make the bank record its fault for all—including the bank examiners—to see.

President Roosevelt, in the same letter to Congress previously mentioned, said: "This proposal [Securities

Act of 1933] adds to the ancient rule of 'caveat emptor' the further doctrine 'let the seller beware.' It puts *the burden of telling the whole truth on the seller.* It should give some impetus to honest dealing in securities and thereby bring back public confidence."[13] If the investors are forced to show in the bank records that the bank intended to defraud them, the burden is unfairly shifted to the innocent party when it should be the seller-lender who bears the burden of fair dealing.

If the issue was the unrecorded representation that the stock was worth more than it actually was, there would be no problem in the application of *D'Oench, Duhme.* As the Court correctly points out, "No authority suggests a right to be compensated by the federal government because one's investments fail." However, investors have the right to expect the protection of federal statutes when the failure comes about due to the actions of the lending bank in connection with the sale of stock.

There were no secret agreements exchanged which excused the payment of the notes. What excuses payment is the conduct of the lending bank in violation of the Securities Act. Nothing in *D'Oench, Duhme* would require the statutorily defrauded borrower-victim to attempt to comply with the recording requirements. *D'Oench, Duhme* ought not to apply because the investors are not trying to enforce a secret or an unwritten agreement but rather are seeking to enforce a statutory right to fair dealing.

II.

The reason that the federal common law would estop state and common law fraud defenses is simply because

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13. H.R. Report No. 85, 73rd Cong. 1st sess., ____ (1933) (italics added).

there is an overriding public policy consideration for a uniform federal rule when dealing with the FDIC.[14] In the leading 5th Circuit case, *Beighley v. FDIC*, 868 F.2d 776 (5th Cir. 1989), the court held that a plaintiff cannot assert fraud claims based on state or common law.

The FDIC says that there is no reason why this should not be extended to federal law fraud claims. They forget the principal reasons why these claims are barred in the first place, namely for the sake of uniformity and the necessity of the FDIC's reliance on the bank records. There is no reason why a fraud claim based on violations of the Securities Act should be barred. The need for uniformity is fulfilled by the fact that this is a *federal* statute, subject only to the vagaries of thirteen Federal Courts of Appeals with the ever present Moderators at the top.

The FDIC will still be able to rely on the bank records which would be available on the supposition that the lending bank is not required to make and keep the records of its own fraudulent conduct. The Holder in Due Course language in § 29 of the Securities Act protects the FDIC.[15] If the FDIC has actual knowledge of the federal security violation, it would not have to rely on those particular debts of the bank until a court decides if they are in fact valid.

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14. "The Federal policy of uniformity of decision for cases arising under federal law would be obviated by a great diversity in results if identical transactions were subject to the vagaries of the laws of several states. Where such inconsistency in decisions would occur, state law is not an appropriate selection to aid in fashioning federal common law." *Clearfield Trust Co. v. United States*, 318 U.S. 363, 367 (1943), quoted from, Norcross, *The Bank Insolvency Game: FDIC Superpowers, The D'Oench Doctrine, and Federal Common Law*, 103 Banking L.J. 316, 343 (1986).

15. See *supra* note 8.

I must emphasize that allowing the Securities Act as a defense to the repayment of loans acquired by the FDIC is a very narrow exception to the *D'Oench, Duhme* doctrine and § 1823(e). In the vast majority of cases, the act will not be available. And even when Securities Act fraud is involved, the actual knowledge requirement will be a tough hurdle to overcome. The Court's concern about excessive litigation is well taken, but in this case, unfounded.

Two policies collide—the policy assuring full knowledge of bank regulators, and the policy of assuring fair dealing in the sale of securities. Until Congress expressly makes the choice, I would hold that violation of the Securities Act is a defense (or basis for affirmative relief) which neither *D'Oench, Duhme* nor § 1823(e) cuts off.

To the Court's failure to so hold, I respectfully dissent.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

CIVIL ACTION NO. H-88-1826

WADE KILPATRICK, STAN E. GOLUB, RICHARD HOWARD, NANCY NORMAN, VICTOR ROGERS, and LOREN SINGLETARY,
Plaintiffs,

v.

JOHN C. RIDDLE, FEDERAL DEPOSIT INSURANCE CORPORATION AS RECEIVER FOR FIRST REPUBLICBANK HOUSTON, N.A., and NCNB TEXAS NATIONAL BANK,
Defendants.

FINAL SUMMARY JUDGMENT

The Court has considered the Defendants/Counter-Plaintiffs' Motion for Summary Judgment filed in the above-entitled-and-numbered cause by the Federal Deposit Insurance Corporation as Receiver for First RepublicBank Houston, N.A., and NCNB Texas National Bank, together with the summary judgment evidence and arguments of counsel. The Court is of the opinion and finds that there are no material issues of fact and that Defendants/Counter-Plaintiffs are entitled to Summary Judgment in their favor as a matter of law. Consequently, the Court is of the opinion and finds that the Defendants/Counter-Plaintiffs' Motion for Summary Judgment should be and is hereby granted. It is therefore

ORDERED that Defendants Federal Deposit Insurance Corporation as Receiver for First RepublicBank Houston, N.A., and NCNB Texas National Bank have Summary Judgment in their favor and that all Plaintiffs take nothing on their affirmative claims for relief. It is further

ORDERED that Defendant/Counter-Plaintiff NCNB Texas National Bank have judgment against Plaintiff/Counter-Defendant Richard Howard for THREE HUNDRED THIRTY-TWO THOUSAND SEVEN HUNDRED SIXTY-ONE AND 42/100 DOLLARS ($332,761.42), representing the outstanding principal ($308,456.72) and accrued interest through March 30, 1989 ($24,304.70) owing on the Howard Note 1, plus additional interest of NINETY-SEVEN AND 19/100 DOLLARS ($97.19) per day, reflecting a contracted for rate of interest, as defined in the Howard Note 1, of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus TWO HUNDRED NINETY-NINE THOUSAND NINE HUNDRED FOUR AND 88/100 DOLLARS ($299,904.88), representing the outstanding principal ($278,000.00) and accrued interest through March 30, 1989 ($21,904.88) owing on the Howard Note 2, plus additional interest of EIGHTY-SEVEN AND 59/100 DOLLARS ($87.59) per day, reflecting a contracted for rate of interest, as defined in the Howard Note 2, of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus SIXTY-TWO THOUSAND THIRTY AND 68/100 DOLLARS ($62,030.68), representing the outstanding principal ($57,500.00) and accrued interest through March 30, 1989 ($4,530.68) owing on the Howard Note 3, plus additional interest of EIGHTEEN AND 12/100

DOLLARS ($18.12) per day, reflecting a contracted for rate of interest, as defined in the Howard Note 3, of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus its costs of court, plus interest as allowed pursuant to 28 U.S.C. § 1961 at the rate of 8.16 percent per annum on all the aforesaid sums from the date of judgment until paid. It is further

ORDERED that Defendant/Counter-Plaintiff NCNB Texas National Bank have judgment against Plaintiff/Counter-Defendant Stan Golub for ONE HUNDRED TEN THOUSAND SEVEN AND 20/100 DOLLARS ($110,007.20), representing the outstanding principal ($100,125.00) and accrued interest through March 30, 1989 ($9,882.20) owing on the Golub Note, plus additional interest of THIRTY-ONE AND 55/100 DOLLARS ($31.55) per day, reflecting a contracted for rate of interest, as defined in the Golub Note, of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus ONE HUNDRED SEVENTY-TWO THOUSAND FIVE HUNDRED AND NO/100 DOLLARS ($172,500.00), representing the amount owing on the Golub Guaranty, plus its costs of court, plus interest as allowed pursuant to 28 U.S.C. § 1961 at the rate of 8.16 percent per annum on all of the aforesaid sums from the date of judgment until paid. It is further

ORDERED that Defendant/Counter-Plaintiff NCNB Texas National Bank have judgment against Plaintiff/Counter-Defendant Nancy Norman for TWO HUNDRED NINE THOUSAND FOUR HUNDRED FIVE AND 97/100 DOLLARS ($209,405.97), representing the out-

standing principal ($195,000.00) and accrued interest through March 30, 1989 ($14,405.97) owing on the Norman Note 1, plus additional interest of SIXTY-ONE AND 44/100 DOLLARS ($61.44) per day, reflecting a contracted for rate of interest, as defined in the Norman Note 1 of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus THIRTY-TWO THOUSAND FOUR HUNDRED FIFTEEN AND 62/100 DOLLARS ($32,415.62), representing the outstanding principal ($30,000.00) and accrued interest through March 30, 1989 ($2,415.62) owing on the Norman Note 2, plus additional interest of NINE AND 45/100 DOLLARS ($9.45) per day, reflecting a contracted for rate of interest, as defined in the Norman Note 2, of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus its costs of court, plus interest as allowed pursuant to 28 U.S.C. § 1961 at the rate of 8.16 percent per annum on all of the aforesaid sums from the date of judgment until paid. It is further

ORDERED that Defendant/Counter-Plaintiff NCNB Texas National Bank have judgment against Plaintiff/Counter-Defendant Victor Rogers for TWO HUNDRED TWENTY-TWO THOUSAND FOUR HUNDRED NINETY-ONE AND 31/100 DOLLARS ($222,491.31), representing the outstanding principal ($195,894.00) and accrued interest through March 30, 1989 ($26,597.31) owing on the Rogers Note 1, plus additional interest of SIXTY-ONE AND 72/100 DOLLARS ($61.72) per day, reflecting a contracted for rate of interest, as defined in the Rogers Note 1, of prime plus zero percent (0%), subject to change in the prime rate, from March

31, 1989, through the date of judgment, plus ONE HUNDRED THIRTY THOUSAND FIFTY-SEVEN AND 85/100 DOLLARS ($130,057.85), representing the outstanding principal ($120,000.00) and accrued interest through March 30, 1989 ($10,057.85) owing on the Rogers Note 2, plus additional interest of THIRTY-SEVEN AND 81/100 DOLLARS ($37.81) per day, reflecting a contracted for rate of interest, as defined in the Rogers Note 2, of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus its costs of court, plus interest as allowed pursuant to 28 U.S.C. § 1961 at the rate of 8.16 percent per annum on all of the aforesaid sums from the date of judgment until paid. It is further

ORDERED that Defendant/Counter-Plaintiff NCNB Texas National Bank have judgment against Plaintiff/Counter-Defendant Loren Singletary for ONE HUNDRED NINETY-TWO THOUSAND SEVEN HUNDRED EIGHTY AND 52/100 DOLLARS ($192,780.52), representing the outstanding principal ($182,875.00) and accrued interest through March 30, 1989 ($9,905.52) owing on the Singletary Note, plus additional interest of THIRTY-ONE AND 55/100 DOLLARS ($31.55) per day, reflecting a contracted for rate of interest, as defined in the Singletary Note, of prime plus zero percent (0%), subject to change in the prime rate, from March 31, 1989, through the date of judgment, plus its costs of court, plus interest as allowed pursuant to 28 U.S.C. § 1961 at the rate of 8.16 percent per annum on all of the aforesaid sums from the date of judgment until paid. It is further

ORDERED that Defendant/Counter-Plaintiff NCNB Texas National Bank have judgment against Plaintiffs/ Counter-Defendants Howard, Golub, Norman, Rogers, and Singletary, jointly and severally, for THIRTY THOUSAND AND NO/100 DOLLARS ($30,000.00), representing the reasonable attorney's fees incurred by NCNB in collecting the Notes and Guaranty at issue in this action, plus interest as allowed pursuant to 28 U.S.C. § 1961 at the rate of 8.16 percent per annum on all of the aforesaid sum from the date of judgment until paid.

SIGNED at Houston, Texas, on this 27th day of July, 1989.

/s/ DAVID HITTNER
David Hittner
United States District Judge

APPENDIX C

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

NO. 89-2963

WADE A. KILPATRICK, ET AL.,
Plaintiffs

STAN E. GOLUB, ET AL.,
Plaintiffs-Appellants,

v.

JOHN C. RIDDLE, ET AL.,
Defendants,

THE FEDERAL DEPOSIT INSURANCE CORP.,
as Receiver for FIRST REPUBLICBANK
HOUSTON, N.A., ET AL.,
Defendants-Appellees.

Appeal from the United States District Court for the
Southern District of Texas

ON SUGGESTION FOR REHEARING EN BANC

(Opinion July 25, 5 Cir., 1990, ____F.2d____)

(August 21, 1990)

Before BROWN, JOLLY and DAVIS, Circuit Judges.

PER CURIAM:

Treating the suggestion for rehearing en banc as a petition for panel rehearing, it is ordered that the petition for panel rehearing is DENIED. No member of the panel nor Judge in regular active service of this Court having requested that the Court be polled on rehearing en banc (Federal Rules of Appellate Procedure and Local Rule 35), the suggestion for Rehearing En Banc is DENIED. ENTERED FOR THE COURT:

/s/ E. GRADY JOLLY
United States Circuit Judge

Judges Jones & Garwood did not participate in the consideration of the suggestion for rehearing en banc.

APPENDIX D

15 U.S.C. § 78cc

§ 78cc. Validity of contracts

Waiver provisions

(a) Any condition, stipulation, or provision binding any person to waive compliance with any provision of this chapter or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void.

Contract provisions in violation of chapter

(b) Every contract made in violation of any provision of this chapter or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this chapter or any rule or regulation thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule, or regulation: *Provided,* (A) That no contract shall be void by reason of this subsection because of any violation of any rule or regulation prescribed pursuant to paragraph (2) or (3) of subsection (c) of section 78*o* of this title, and (B) that no contract shall be deemed to be void by reason of this

subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) of subsection (c) of section 78*o* of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation.

Validity of loans, extensions of credit, and creation of liens; actual knowledge of violation

(c) Nothing in this chapter shall be construed (1) to affect the validity of any loan or extension of credit (or any extension or renewal thereof) made or of any lien created prior or subsequent to the enactment of this chapter, unless at the time of the making of such loan or extension of credit (or extension or renewal thereof) or the creating of such lien, the person making such loan or extension of credit (or extension or renewal thereof) or acquiring such lien shall have actual knowledge of facts by reason of which the making of such loan or extension of credit (or extension or renewal thereof) or the acquisition of such lien is a violation of the provisions of this chapter or any rule or regulation thereunder, or (2) to afford a defense to the collection of any debt or obligation or the enforcement of any lien by any person who shall have acquired such debt, obligation, or lien in good faith for value and without actual knowledge of the violation of any provision of this chapter or any rule or regulation thereunder affecting the legality of such debt, obligation, or lien.

June 6, 1934, c. 404, Title I, § 29, 48 Stat. 903; June 25, 1938, c. 677, § 3, 52 Stat. 1076.

12 U.S.C. § 1823

(e) Agreements against interests of Corporation

No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this section or section 1821 of this title, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—

(1) is in writing,

(2) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution,

(3) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and

(4) has been, continuously, from the time of its execution, an official record of the depository institution.

DEC 3 1990
JOSEPH F. SPANIOL, JR.
CLERK

(2)

NO. 90-692

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

VICTOR ROGERS AND
LOREN SINGLETARY,
Petitioners,

v.

THE FEDERAL DEPOSIT INSURANCE CORP., As Receiver for FIRST REPUBLICBANK HOUSTON, N.A., and NCNB TEXAS NATIONAL BANK,
Respondents.

BRIEF OF RESPONDENT NCNB TEXAS NATIONAL BANK IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTION PRESENTED

Whether the Court of Appeals correctly held that the *D'Oench, Duhme* doctrine precluded alleged federal securities fraud claims and defenses based on conduct of a closed bank.

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BRIEF OF RESPONDENT NCNB TEXAS NATIONAL BANK IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Because the ruling of the Court of Appeals on the narrow issue involved in this case is correct and does not create a conflict among the circuits, and because Congress has resolved the issue raised in this case through passage of the Financial Institutions Reform, Recovery and Enforcement Act of 1989, Respondent NCNB Texas National Bank ("NCNB") respectfully opposes the petition for writ of certiorari in this case.

STATUTES INVOLVED

In addition to the statutes cited in the Petition, this case involves the following statutes, as modified or enacted by the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"):

12 U.S.C. § 1821(d)(9)(A)
12 U.S.C. § 1821(n)(4)(I)
12 U.S.C. § 1823(e)

The text of these statutes is set forth in the appendix to this brief.

STATEMENT

Because the Petition's Statement of the Case is premised on a mischaracterization of the lower courts' handling of the procedural posture of this case and an inaccurate portrayal of the factual record, NCNB is forced to present its own statement of the procedural and factual record on which the decisions of the Court of Appeals and the district court are premised.

1. The Federal Deposit Insurance Corporation as Receiver for First RepublicBank Houston, N.A. ("FDIC") and NCNB were named Defendant, and NCNB counterclaimed seeking recovery on promissory notes and guaranties that it had acquired by assignment from the FDIC. They moved jointly for complete summary judgment promptly after service of this action.

As summary judgment evidence, NCNB and FDIC presented a series of promissory notes and guaranties executed by Petitioners and their co-plaintiffs. NCNB further submitted an affidavit of one of its officers estab-

lishing the accrued amounts owing on the debt instruments and an affidavit of its attorney establishing reasonable fees for collection of those debts. FDIC and NCNB also submitted court records reflecting the appointment of the FDIC as receiver and the acquisition by NCNB of the debt instruments at issue in the case. Those records established that, on July 29, 1988, the Comptroller of the Currency declared First RepublicBank, Houston, N.A. ("FRB Houston"), insolvent and appointed FDIC receiver for the closed bank under 12 U.S.C. § 1821(d); and that on that same day, the FDIC as Receiver, acting pursuant to order of the District Court for the Southern District of Texas, entered into a Purchase and Assumption Agreement with a bridge bank newly formed under what was then 12 U.S.C. § 1821(i) (now codified as amended at 12 U.S.C. § 1821(n)), by which the bridge bank acquired certain assets and assumed certain liabilities of the closed bank from the receiver. The bridge bank was renamed NCNB Texas National Bank; the notes and guaranties in the summary judgment record accordingly reflect that they have been endorsed by the FDIC to NCNB.

The circumstances of the involvement of FDIC and NCNB with Petitioners' debts are therefore clearly established in the summary judgment record. FDIC was required to be appointed receiver under 12 U.S.C. § 1821 (d), and as such was legally obligated to take possession of and marshall all the assets and resolve all the liabilities of the closed bank for the benefit of the creditors and shareholders of the bank; there can be no question but that FDIC acquired Petitioners' debts in absolute good faith. NCNB was obligated by federal law as bridge bank

to acquire those assets assigned to it by the FDIC, 12 U.S.C. § 1821(i) (now (n)); NCNB likewise acquired Petitioners' assets in unquestionable good faith. By assuming responsibility for all the liabilities of the closed bank, FDIC acquired the closed bank's assets, including Petitioners' debt, for real value. By assuming those liabilities of the closed bank that it was required to assume under then 12 U.S.C. § 1821(i) (all deposit liabilities and all liabilities FDIC required it to assume), NCNB as bridge bank also aquired those debts for real value. Last, the summary judgment record established that neither the FDIC *as Receiver* nor NCNB even existed before FRB Houston was closed; by the very nature of the receivership and bridge bank processes, therefore, it was impossible for either entity to have had any knowledge about any circumstances involving the debt assets being acquired. The summary judgment record submitted by FDIC and NCNB, therefore, proved good faith and value and disproved pertinent knowledge.

Neither Petitioners nor any of their co-plaintiffs submitted or pointed out *any* evidence whatsoever in response either to the summary judgment motion of NCNB and FDIC or to the evidence submitted in support of the motion. Petitioners' lengthy recitation of the supposed facts supporting their purported claims and defenses, therefore, finds no support in the summary judgment record. NCNB and FDIC relied pointedly on Petitioners' failure to submit any summary judgment evidence—both before the district court in their reply brief in support of summary judgment, and in their brief in the Court of Appeals—as full justification for the summary judgment they sought (and ultimately obtained).

Petitioners try to cover up this lack of record support for their arguments by advancing the erroneous contention that their "federal securities fraud claims were taken as admitted for purposes of summary judgment." Pet. 2 fn. 1. The district court did not consider Petitioners' claims to have been admitted; to the contrary, the district court's summary judgment order recites that Petitioners had raised "no material issues of fact," Pet. App. 25a. The Fifth Circuit assumed for the sake of argument that Petitioners had "stated a claim for securities fraud against" the closed bank, Pet. App. 10a; this is a mere acknowledgement, however, that Petitioners' allegations might have survived a motion to dismiss, not an indication that Petitioners' bare pleadings were being, or could have been, taken as true for the purposes of the summary judgment motion. To the contrary, the Court of Appeals concluded that its holding on the impact of the *D'Oench, Duhme* doctrine meant that it was "not" necessary to "consider whether there were genuine issues of material fact concerning the alleged fraud." Pet. App. 14a.

In any event, because Petitioners presented no evidence, the summary judgment record contains absolutely no valid proof of any element of Petitioners' purported federal securities claims or defenses or their factual arguments for avoiding *D'Oench, Duhme.* There is even no valid summary judgment evidence of a security or the sale of any stock. There is thus no evidence that Petitioners' debt is in any way connected with a purchase or sale of securities. (Part of Mr. Rogers' debt, for example, is in fact related to his purchase of a title company.) There is no evidence of reliance by either Petitioner on any representation or omission of the closed bank, either in purchasing

any stock or in executing the debt instruments (probably because Petitioners, who were themselves directors of the two Texas National Banks, *see* Petition, p. 3, were promotors of the two bank capitalizations, and because Mr. Rogers was a law partner of individual defendant Riddle, so that neither Petitioner could swear under oath that actions, representations or omissions of the closed bank had anything to do with their decisions to become involved with the Texas National Banks). Most important of all, there is no valid summary judgment evidence of any fraud by anyone, much less deliberate fraud by the closed bank.

Similarly, there is no proof that the FDIC *as Receiver* or NCNB had any actual knowledge of any conduct of the closed bank. Petitioners have never suggested that NCNB could have had any such knowledge. And their arguments that the FDIC had knowledge are based on mere allegations made by the receiver of a different closed bank in pleadings that were, once again, not made part of the summary judgment record (no doubt because the same district court that granted judgment in this case had already dismissed those pleadings with prejudice).

In conclusion, the factual record relevant on this appeal of a summary judgment contains no evidence to support any of the factual claims made in the Petition. For this reason at least, the district court granted the joint motion of FDIC and NCNB for summary judgment. Pet. App. 25a-30a.

2. On appeal, the FDIC and NCNB asserted three grounds for affirmance of the district court decision. First, they noted that this Court's decision in *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986), compelled an award of

summary judgment because Petitioners failed to submit any evidence in opposition to the summary judgment motion. Second, because all of Petitioners' claims and defenses to the debt instruments were based on the alleged fraud of FRB Houston in supposedly failing to tell Petitioners about certain allegedly material aspects of their stock investment in two other failed banks, FDIC and NCNB argued that those claims and defenses would be barred by the principle announced by this Court in *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942). Last, the FDIC and NCNB argued that the circumstances of their possession and ownership of the debt instruments executed by Petitioners required that they be deemed protected as a matter of law by Section 29(c) of the Securities and Exchange Act, 15 U.S.C. § 78cc(c), the "innocent purchaser" provision of the federal securities laws.

The Court of Appeals addressed only the second issue, affirming on the basis of *D'Oench, Duhme*. The court acknowledged that the "oral side agreement" at issue in *D'Oench* had become the paradigmatic "secret agreement" barred by the [*D'Oench, Duhme*] doctrine. Pet. App. 6a. It further noted that in *Langley v. FDIC*, 484 U.S. 86 (1987), this Court had more recently rejected a narrow interpretation of the category of "agreements" governed by the federal common law doctrine and its statutory counterpart 12 U.S.C. § 1823(e), and had held that any unwritten condition to an unqualified promise to repay is just such an agreement, even if the condition, like the condition to repayment posited by Petitioners, is the "truthfulness of a warranted fact," *id.* at 93. Pet. App. 8a-10a.

The Court of Appeals could find no reason to create an exception to the *D'Oench, Duhme* doctrine merely because the fraudulent inducement involved transactions governed by the federal securities laws. It noted that "[e]xcept for the fact that the asset [securing the debt instruments] in this case is stock rather than land, and its sale thus regulated by federal law," this case is "essentially indistinguishable" from *Langley*. Pet App. 11a. The court acknowledged that only one prior court had expressly rejected federal securities claims "on the basis of the *D'Oench, Duhme* doctrine," and that other courts had skirted the issue, but also noted that similar state securities claims had been rejected under the doctrine. Pet. App. 11a-12a. The court further reasoned that enforcement of the federal securities laws would not be threatened by straightforward application of the *D'Oench, Duhme* doctrine. Blocking Petitioners federal securities claims against the FDIC, and precluding federal securities defenses against collection by NCNB, would "not deprive [them] of protection under the federal securities laws because borrowers can always sue"—as Petitioners did in this case —"the individuals who actually defrauded them." Pet. App. 12a-13a. The court concluded by quoting the reasoning of a prior panel that application of the *D'Oench, Duhme* doctrine merely " 'favors the interests of depositors and creditors of a failed bank, who cannot protect themselves from secret agreements, over the interests of borrowers, who can.' *Campbell Leasing, Inc. v. FDIC*, 901 F.2d 1244, 1248 (5th Cir. 1990)." Pet. App. 13a.

SUMMARY OF REASONS FOR DENYING THE WRIT

There is no reason to grant a writ of certiorari to review the Court of Appeals' faithful application of settled precedent of this Court in the narrow context of this case.

1. The decision of the Court of Appeals that the *D'Oench, Duhme* doctrine precludes certain federal securities fraud claims and defenses does not conflict with applicable decisions of this Court. The panel's reliance on the decision in *D'Oench, Duhme* fully conforms with this Court's subsequent decision in *Langley* and clearly does not conflict with decisions of this Court that predate, and thus do not even address, the *D'Oench* decision. This Court, moreover, has recently reaffirmed that common law defenses may be available in limited situations to defeat express and implied statutory securities fraud claims. The *D'Oench, Duhme* doctrine is just such a narrow federal common law principle, and the Court of Appeals faithfully analyzed and correctly resolved the issues this Court has identified for determining the applicability of common law defenses to federal securities claims.

2. The decision of the Court of Appeals does not conflict with the decision of any other Court of Appeals on the same matter. The decision of the Fifth Circuit in this case is entirely consistent with decisions of the Sixth Circuit that are directly on point, and appears to be consistent with an almost contemporaneous decision of the Tenth Circuit ruling that undefined securities fraud claims and defenses are not valid when asserted against the FDIC. The decision of the Court of Appeals in this case does not involve allegations of insider trading, so that it does not

conflict with the Eighth Circuit's decision that an insider trading claim is not barred by the *D'Oench, Duhme* doctrine. And the decision of the Court of Appeals in this case does not conflict with the decisions of the Eleventh Circuit in which the Eleventh Circuit declined to apply *D'Oench* to defeat federal securities fraud claims, but ruled in favor of FDIC or its assignee on the basis of other defenses to the federal securities claims. Nor does the decision below conflict with the decision of the Fourth Circuit that ruled in favor of the FDIC on the basis of a different common law defense to federal securities claims.

3. The narrow issue decided by the Court of Appeals is no longer an important question of federal law and thus does not need to be settled by this Court. Whether the *D'Oench, Duhme* doctrine defeats a federal securities law claim is an issue that arises only in the limited group of cases that contain federal securities fraud claims against a closed bank or federal securities fraud defenses against collection of a note acquired by or from an FDIC receiver. Even in this limited group of cases, plaintiffs are highly unlikely to succeed against the FDIC as Receiver or its assignee because the very nature of the receivership and assignment processes should enable FDIC and its assignees to rely in any event on the defenses and protections that are already express provisions of the federal securities laws. Since the institution of this lawsuit, moreover, Congress has passed FIRREA, which directly addresses with express statutory provisions the issue that the Court of Appeals decided under the federal common law *D'Oench, Duhme* doctrine. Future litigation will therefore not be impacted at all by the resolution of the narrow issue decided by the Court of Appeals.

4. The peculiar procedural posture of this case also makes it inappropriate for review by this Court. Petitioners' failure to present summary judgment evidence makes review by this Court difficult at best. The Court of Appeals, moreover, did not address two separate issues that NCNB contends are each separately and independently dispositive of this case. First, because the summary judgment record makes clear that Petitioners did not even attempt to raise a genuine issue of material fact on their federal securities claims, NCNB and FDIC were entitled to summary judgment on this ground alone, without reference to the *D'Oench, Duhme* doctrine. Second, the summary judgment record establishes that NCNB and FDIC were entitled as a matter of law to defeat Petitioners' federal securities claims under the express innocent purchaser provisions of the federal securities laws themselves. For these reasons as well, further review by this Court is not warranted.

REASONS FOR DENYING THE WRIT

1. The Decision Below Is Correct and Does Not Conflict with Any Decision of This Court

The Court of Appeals applied *D'Oench, Duhme* and *Langley* in a straightforward manner and correctly concluded that the *D'Oench, Duhme* doctrine is applicable to the unwritten condition to repayment of their debts posited by Petitioners which, though based on the federal securities laws, is indistinguishable from any other claim of fraudulent inducement that is governed by the doctrine. Petitioners argue that the decision below "stretches the meaning of the term 'agreement' beyond all reasonable limits" because under that decision, "virtually no condi-

tion not spelled out in a promissory note can defeat the FDIC's right to collect . . . since *any* common law *or* state *or* federal statutory [defense] automatically counts as a 'secret agreement' not to repay the note." Pet. 10 (emphasis in original). What Petitioners fail to recognize is that this very conclusion is compelled by this Court's decision in *Langley v. FDIC*, 484 U.S. 86 (1987). There this Court expressly held that any "condition to repayment of a note, including the truth of an express warranty [or implied representation], is part of the 'agreement' to which the" statutory counterpart of *D'Oench, Duhme* applies. *Id.* at 96.

Petitioners repeatedly attempt to criticize the Court of Appeals in effect for its decision, Pet. App. 10a-11a, to deem prior knowledge of the FDIC irrelevant for the purposes of applying *D'Oench, Duhme*. *See* Pet. 15, 17. This Court's decision in *Langley* again disposes of this argument, holding unequivocally that knowledge of the FDIC is simply "not relevant." 484 U.S. at 94.

Petitioners also contend that the decision below conflicts with this Court's decision in *Oppenheimer v. Harriman Nat'l Bank & Trust Co.*, 301 U.S. 206 (1937). Because the *Oppenheimer* case predates *D'Oench, Duhme*, however, the *Oppenheimer* decision does not even address the possible defenses available to FDIC to defeat a federal securities claim. The *Oppenheimer* case, moreover, concerned a bank's sale of its own stock, not a loan made to purchase stock in a different bank. In any event, as the Court of Appeals correctly noted, Pet. App. 5a n.3, the *Oppenheimer* decision "says nothing about [the] ability of [a bank shareholder] to recover from a federal receiver."

Petitioners last contend that the express provisions of the federal securities laws preclude common law defenses. Pet. 12-15. Once again, however, Petitioners' argument has been firmly rejected by recent decisions of this Court. It is true that this Court has acknowledged "the inappropriateness of invoking broad common-law barriers to relief where a private suit serves important public purposes." *Perma Life Mufflers, Inc. v. International Parts Corp.*, 392 U.S. 134, 138 (1968). Even in *Perma Life*, however, a majority of this Court concluded that some limited common law defense based on comparative fault (*in pari delicto*) would be available even under the antitrust laws. *See Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 309 (1985). This Court in *Bateman Eichler* then established a two-prong test for determining whether a common law *in pari delicto* defense should be available in a federal securities case, requiring an analysis of 1) comparative fault; and 2) the impact of allowing the defense on federal securities law enforcement. *Id.* at 310-11. This Court has subsequently held that the *Bateman Eichler* analysis applies in determining whether the *in pari delicto* defense can be raised against any federal securities claim, express or implied. *Pinter v. Dahl*, 108 S. Ct. 2063 (1988). There can be no question, therefore, that in limited circumstances certain common law defenses can preclude federal securities law claims of any nature.

In deciding that the *D'Oench, Duhme* doctrine did preclude federal securities fraud claims and defenses, the Court of Appeals in effect applied the *Bateman Eichler* two-prong test, and applied the test correctly. The decision below properly balances the fault of Petitioners—who purported to rely on an unwritten condition to their debts and thus participated in a scheme that would tend to

mislead bank examiners—with the plain innocence of the FDIC-Receiver, as protector of the insurance fund and representative of the innocent creditors and shareholders of the closed bank—none of whom participated in the alleged wrongdoing of the closed bank. *See* Pet. App. 13a. The decision below likewise expressly, and accurately, concludes that federal securities law enforcement will not be impeded if the *D'Oench, Duhme* bars federal securities fraud claims, because a closed bank's borrowers can always sue any wrongdoer other than the closed bank. Pet. App. 2a, 12a-13a.

Because the decision below correctly applies settled precedent in this Court, review by this Court is not warranted.

2. The Decision Below Does Not Conflict with Any Decision of Another Court of Appeals

Petitioners erroneously contend that the decision below conflicts with holdings of other Courts of Appeal. Pet. 15-20. As Petitioners' own analysis indicates, there is no such conflict.

The decision below correctly notes that the Sixth Circuit, the only other Court of Appeals to address the issue directly, concluded that the *D'Oench, Duhme* doctrine bars "federal securities law defenses," *FDIC v. Investors Associates X, Ltd.*, 775 F.2d 152, 156 (6th Cir. 1985). Pet. App. 12a. Petitioners attempt to conjure up a conflict with the Sixth Circuit's decision in *Gilman v. FDIC*, 660 F.2d 688 (6th Cir. 1981). Pet. 17. The court in *Gilman*, however, expressly held that "the interests of conformity compel" identical results in federal securities and

common law fraud cases. *Id.* at 695. There is no conflict with any decision of the Sixth Circuit.

In a recent case, moreover, the Tenth Circuit rejected "securities and common law fraud" counterclaims under the *Langley* decision. *FDIC v. Bell*, 892 F.2d 64, 65 (10th Cir. 1989), *cert. dismissed*, 110 S.Ct. 2067 (1990). If anything, therefore, at least two other courts of appeal (the Sixth and Tenth Circuits) have expressly agreed with the decision below.

Petitioners also seek to manufacture a conflict between the decision below and the Eighth Circuit's recent decision in *Astrup v. Midwest Federal Savings Bank*, 886 F.2d 1057 (8th Cir. 1989). *See* Pet. 18-19. There the Eighth Circuit held that *D'Oench, Duhme* would not defeat a claim under the federal securities laws for insider profits because such a claim sounded in tort. *Id.* at 1059-60. Petitioners, however, make no insider trading claim, which would be in the nature of a conversion claim rather than a fraudulent inducement claim. As this Court held in *Langley*, a fraudulent inducement claim necessarily posits an undisclosed agreement that payment on an otherwise unconditional note is conditioned on the truthfulness of represented fact. 484 U.S. at 93. A fraudulent inducement claim under the federal securities laws is therefore premised on contract and is accordingly plainly prohibited by *D'Oench, Duhme*, even under the reasoning of the Eighth Circuit in *Astrup*. *See* 886 F.2d at 1059. There is no conflict with the Eighth Circuit.

The Eleventh Circuit has twice "declined" to apply *D'Oench, Duhme* to bar federal securities fraud claims or defenses. *Vernon v. RTC*, 907 F.2d 1101, 1108 (11th Cir. 1990); *Gunter v. Hutcheson*, 674 F.2d 862, 877 (11th Cir.) *cert. denied*, 459 U.S. 826 (1982). In *Vernon*, the Eleventh Circuit found it "unnecessary" so to "extend

the *D'Oench* doctrine," because it rejected the federal securities fraud claims against the assignee of the receiver of a failed savings and loan on the basis that the assignee had not assumed that potential liability in its transaction with the receiver. 907 F.2d at 1108. In *Gunter*, the Eleventh Circuit likewise held it unnecessary to apply *D'Oench, Duhme* "in this case," because it rejected the federal securities fraud defenses on other grounds. 674 F.2d at 877. (The *Gunter* analysis of 12 U.S.C. § 1823 (e) was, moreover, rejected by this Court in *Langley*.) Contrary to the arguments of Petitioners, Pet. 16-17, 19-20, there is no conflict between the decision below and the decisions of the Eleventh Circuit in *Vernon* and *Gunter*.

Petitioners' final effort to find a conflict in the circuits purports to rely on the Fourth Circuit's decision in *FDIC v. Aroneck*, 643 F.2d 164 (4th Cir. 1981). There the FDIC did not even raise *D'Oench, Duhme*, because it was able to prevail by establishing an *in pari delicto* defense, as Petitioners acknowledge. Pet. 18. There is no conflict at all between the decision below and the decision in *Aroneck;* each Court of Appeals simply chose to address different issues, but decided in favor of FDIC in either event.

Review is not needed to resolve any conflict in the circuits.

3. Review by This Court Is Not Warranted on the Narrow Issue of Law Underlying the Decision Below, Which Has Been Made Moot in Any Event by Subsequent Congressional Action

The issue resolved in the decision below is a narrow one that will have arisen only in rare circumstances. There

must be a claim or defense based on fraudulent inducement in connection with the purchase of a security. A failed financial institution must have been a legitimate defendant. As Judge Brown admitted in his dissent:

> In the vast majority of cases, the [federal securities laws] will not be available [when *D'Oench, Duhme* is involved]. And even when Securities Act fraud is involved, the actual knowledge hurdle [of § 29(c) of the Securities and Exchange Act] will be a tough hurdle to overcome.

Pet. App. 24a. Review by this Court is therefore unwarranted on a narrow issue of such limited importance.

In any event, review is not warranted because of changes in the banking laws enacted by Congress through the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Publ. L. No. 101-73, 103 Stat. 183. As the court of appeals noted (see Pet. App. 7a and note 4), prior to 1989, 12 U.S.C. § 1823(e) applied only when the FDIC was acting in its corporate capacity and not when it was acting as a receiver. But Section 1823(e) was amended in 1989 to apply as well when, as here, the FDIC is acting "as receiver of any insured depository institution." 103 Stat. 256. In addition, Congress added 12 U.S.C. § 1821(d)(9)(A), which states that "any agreement which does not meet the requirements set forth in section 1823(e) of this title shall not form the basis of, or substantially comprise, a claim against the receiver or the Corporation." § 212, 103 Stat. 231. Congress also added 12 U.S.C. § 1821(n)(4)(I), which applies the four requirements of section 1823(e) to any asset acquired by a bridge bank like NCNB. 103 Stat. 249. In the future there will be no question that federal securities

fraud claims and defenses will be barred by these statutory provisions.

4. The Procedural Posture of This Case and the State of Its Record Make It Inappropriate for Review by This Court

Petitioners unfairly criticize the Court of Appeals for having "recast" their claims and defenses as fraudulent inducement claims and defenses when in fact they are claims based on allegedly fraudulent sales of securities. Pet. 8-11. Instead, it is Petitioners themselves who are to blame for any mischaracterization, for it is they who failed to present any summary judgment evidence to support those claims, however they might be characterized. For this reason alone, the record in this case is not adequate to support meaningful review by this Court.

The plain truth, moreover, is that Petitioners' claims against FDIC are *not* based on the sale of securities, because FRB Houston did not sell any of the stock in the Texas National Banks, and Petitioners do not allege that it did. If the claims had any factual foundation at all, they were based on the closed bank's supposed fraudulent inducement of the execution of Petitioners' notes and guaranties. It is for this reason that Petitioners conceded below that their *common law* fraud claims were indeed barred by *D'Oench, Duhme*: Petitioners' claims and defenses are premised on fraudulent inducement. The Court of Appeals, therefore, correctly characterized Petitioners' claims and defenses. Review is plainly not warranted on this ground.

Review is also not warranted because FDIC and NCNB raised valid grounds for affirming summary judgment independent of the narrow ruling of the Court of Appeals.

Specifically, summary judgment was warranted under both Rule 56 of the Federal Rules of Civil Procedure and Section 29(c) of the Securities & Exchange Act.

Rule 56(c) of the Federal Rules of Civil Procedure provides that a district court "shall" grant summary judgment when the summary judgment record shows no genuine issues for trial and the movant's right to judgment as a matter of law. In *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986), this Court held that:

> The plain language of Rule 56(c) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which the party will bear the burden of proof at trial.

In other words, on issues like all the elements of Petitioners' federal securities defenses to the debt instruments and all the elements of their affirmative federal securities claims, on which Petitioners would have borne the burden of proof at trial, Petitioners were required "to go beyond the pleadings and . . . designate 'specific facts showing that there is a genuine issue for trial'." *Id.* at 324, *quoting* Fed. R. Civ. P. 56(e); *accord, Lujan v. National Wildlife Federation*, 110 S.Ct. 3177, 3188 (1990). Because Petitioners offered no summary judgment evidence, however, they raised no genuine issue of fact with respect to any element of their purported federal securities laws claims or defenses. There is no evidence of a security, no evidence of fraud, no evidence of reliance by any Plaintiff. For this reason alone, the district court properly rendered summary judgment.

Section 29(c) of the Securities and Exchange Act, provides, in effect, that no violation of the federal securities law may serve as a defense to any debt or obligation against "any person who shall have acquired such debt [or] obligation . . . in good faith for value and without actual knowledge of the violation." 15 U.S.C. § 78cc(c). As a consequence of the receivership and bridge bank processes, as established in the summary judgment record, both the FDIC as Receiver and NCNB in fact acquired Petitioners' debts in good faith for value and without actual knowledge of any federal securities violation by FRB Houston. As a matter of law, FDIC and NCNB were innocent purchasers under Section 29(c). For this reason as well, summary judgment was entirely proper.

CONCLUSION

For the foregoing reasons, there is no valid reason to grant the writ. The Petition for Writ of Certiorari in this case should be denied.

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APPENDIX

12 U.S.C. § 1821(d)(9(A)

(9) Agreement as basis of claim

(A) Requirements

Except as provided in subparagraph (B), any agreement which does not meet the requirements set forth in section 1823(e) of this title shall not form the basis of, or substantially comprise, a claim against the receiver or the Corporation.

12 U.S.C. § 1821(n)(4)(I)

(4) Powers of bridge banks

Each bridge bank chartered under this subsection shall have all corporate powers of, and be subject to the same provisions of law as, a national bank, except that—

(I) no agreement which tends to diminish or defeat the right, title or interest of a bridge bank in any asset of an insured bank in default acquired by it shall be valid against the bridge bank unless such agreement—

(i) is in writing,

(ii) was executed by such insured bank in default and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by such insured bank in default,

(iii) was approved by the board of directors of such insured bank in default or its loan committee, which approval shall be reflected in the minutes of said board or committee, and

(iv) has been, continuously from the time of its execution, an official record of such insured bank in default;

12 U.S.C. § 1823(e)

(e) Agreements against interests of Corporation

No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this section or section 1821 of this title, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—

(1) is in writing,

(2) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution,

(3) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and

(4) has been, continuously, from the time of its execution, an official record of the depository institution.

(3)

NO. 90-692

Supreme Court, U.S.
FILED
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JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

VICTOR ROGERS and
LOREN SINGLETARY,
Petitioners,

v.

THE FEDERAL DEPOSIT INSURANCE CORP.,
As Receiver for
FIRST REPUBLICBANK HOUSTON, N.A.
and NCNB TEXAS NATIONAL BANK,
Respondents

PETITIONERS' REPLY TO RESPONDENT NCNB TEXAS NATIONAL BANK'S OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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December 11, 1990

QUESTION PRESENTED

Whether the federal common law *D'Oench, Duhme* doctrine shields the FDIC and the successor to a failed financial institution from federal securities law claims—particularly claims under § 29 of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc.

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IN THE

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THE FEDERAL DEPOSIT INSURANCE CORP.,
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and NCNB TEXAS NATIONAL BANK,
Respondents

PETITIONERS' REPLY TO RESPONDENT NCNB TEXAS NATIONAL BANK'S OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Because the Brief in Opposition to Petitioners' Petition for Writ of Certiorari (the "Petition") filed by Respondent NCNB Texas National Bank ("NCNB") raises new issues which seriously misstate both fact and law, Petitioners Rogers and Singletary file this Reply to NCNB's Brief in Opposition ("Opposition") and respectfully show the Court the following:

NEW ISSUES RAISED IN NCNB'S BRIEF IN OPPOSITION MISREPRESENT BOTH FACT AND LAW.

1. Respondent NCNB Claims For The First Time And Without Any Legal Or Factual Foundation That The Common Law *In Pari Delicto* Defense Actually Governs This Case And Precludes Petitioners' Claims.

It is interesting to compare how Petitioner and Respondent each frame the issue presented by this case. The difference explains much of the need for this Reply. Respondents NCNB claims that there is no conflict in the Circuit Court over the question posed by this case and that this case was correctly decided by the Fifth Circuit Court of Appeals under settled law. Opposition at 14-16, 11-13. This Court can assess for itself the merits of Petitioners' claim and Respondent's denial that there is a conflict in the circuits regarding the preclusion of federal securities law claims by the federal common law *D'Oench, Duhme* doctrine. Petition at 15-20; Opposition at 14-16. However, NCNB introduces in its Brief the novel notion that the law governing this case is settled because the common law *in pari delicto* defense—a defense *never* pled in this *D'Oench, Duhme* case and never addressed in any pleading or brief in any evidence presented to any court, or in any opinion issued below—actually governs this case and was correctly applied by the Court of Appeals. Opposition at 13. According to NCNB, the Fifth Circuit (without ever saying so) was actually balancing the fault of Petitioners as victims of NCNB's fraud against the innocence of the FDIC when it rejected Petitioners' claims in a split decision on the basis of what it said was the *D'Oench, Duhme* doctrine. Opposition at 13-14. Aside from the interjection of a "governing" defense never raised in this case, Respondent seems to be arguing that the complex statutory scheme of federal securities law recognizes one common law de-

fense, *in pari delicto;* therefore, federal common law bars federal securities law claims—a logical non-sequitur.

In actuality, Respondent's claim that this case is really nothing but a correct application of the settled law of *in pari delicto* is but one of many examples of Respondent's attempts to sweep aside both Petitioners' actual claims and the actual holdings of the courts below and to recast all those claims and holding to Respondent's liking. Thus this Court's recognition of one (non-applicable) common law defense to federal securities claims becomes "settled law" holding that federal common law overrides federal securities law; the federal common law *D'Oench, Duhme* doctrine becomes the common law *in pari delicto* doctrine; *D'Oench, Duhme* defenses become, at Respondent's whim, federal statutory defenses under 12 U.S.C. § 1823(e) or the Financial Institution Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 ("FIRREA"); the fraudulent sale of securities in violation of federal statute becomes common law fraudulent inducement; and so on. This blatant manipulation of actual issues to Respondent's taste is unauthorized in law, unjustified on the facts, and dangerous in application. It should be rejected out of hand by this Court in every guise in which Respondent has advanced it. Accordingly, since Respondent's claim that this case is controlled by settled law boils down to the claim that Petitioners' claims are precluded by the common law defense of *in pari delicto,* Respondent's argument that the case is controlled by settled law should be rejected.

2. Respondent NCNB Incorrectly Claims That The Decision Below Has Been Moved By A Subsequent Congressional Act.

Respondent NCNB claims that the decision below has been mooted by FIRREA's extension of the provisions of § 1823(e) to cases like this one in which the FDIC is present as receiver. Opposition at 17-18. The claim that FIRREA extends § 1823(e) to the FDIC as receiver is true and undisputed, although § 1823(e) has not been pled by Respondents in this case. The further claim that FIRREA moots *D'Oench, Duhme* is false. The *D'Oench Duhme* doctrine has never been held to have been precluded by § 1823(e), either in its pre-FIRREA guise or in its post-FIRREA guise. To the contrary, the federal courts, including this Court, have uniformly held or assummed that the *D'Oench, Duhme* doctrine and § 1823(e) are complimentary defenses and have applied them jointly or singly as appropriate. *See FDIC v. McClanahan,* 795 F.2d 512, 514, n.1 (5th Cir. 1986) (§ 1823(e) does not preempt the common law rule of *D'Oench, Duhme*); see *also Langley v. FDIC,* 484 U.S. 86 (1987) and *Gunter v. Hutchinson,* 674 F.2d 862 (11th Cir.), *cert. denied,* 459 U.S. 826 (1982). Moreover, Respondent's further claim that, "In the future there will be no question that federal securities fraud claims and defenses will be barred" by § 1823(e) and by 12 U.S.C. § 1821(a)(4)(I) (which extends the provisions of § 1823(e) to bridge banks like NCNB) is without legal support. *See* Opposition at 17-18. This Court has never held that § 1823(e)—either pre- or post-FIRREA law—or § 1821 shields the FDIC or any successor to a failed financial institution from federal securities law claims. Therefore that important question remains to be answered, and Respondents' preemptory claim that "there will be no question that federal securities fraud claims and defenses will be barred" is nothing more than a naked assertion unsupported by law and provides no ground for denying certiorari.

3. Respondent NCNB Incorrectly Claims That This Case Is Procedurally Defective.

Respondent NCNB makes much of a supposed procedural defect in the posture of this case, allegedly deriving from Petitioners' failure to prove fraud at the summary judgment level. Opposition at 2-6, 18-19. Respondent NCNB raised the same claim for the first time on appeal in the Fifth Circuit, where it was fully briefed and was rejected by the Circuit Court. *See* Pet. App. at 10a. Nor could Respondent have prevailed on its claim. Respondents NCNB and FDIC rested their entire motion for summary judgment on the *legal* claim that the federal common law *D'Oench, Duhme* doctrine precludes fraud, including federal securities fraud, as a defense to collection of notes executed in favor of a failed bank. On their own theory of the case, proof of fraud in such cases is *immaterial* and cannot prevent the rendition of summary judgment in favor of the FDIC and the successors to a failed institution under *D'Oench, Duhme*. Respondent NCNB admitted as much in its Brief in Support of Motion for Summary Judgment at 18, stating, "fraud, federal securities, states securities, waiver and estoppel claims are all immaterial to recovery by NCNB." Had fraud, in fact, been material to Respondent's Motion for Summary Judgment, *Respondent* not Petitioners would have had the burden of proving the *non-existence* of fraud before the burden shifted to Petitioners to prove its existence. *Adicks v. S.H. Kress & Co.*, 398 U.S. 144, 159-160, 90 S. Ct. 1598, 1609 (1970). Where the movant for summary judgment does not meet its initial burden of establishing the absence of material fact, the non-movant is not required to come forward with suitable opposing affidavits. *Adicks*, 398 U.S. at 160, 90 S. Ct. at 1610. In fact, Respondents did not challenge Petitioners' statement of the

facts, and, therefore, the court was required to interpret those facts in the light most favorable to Petitioners. *See* 398 U.S. at 158-159, 91 S. Ct. at 1609. The Court of Appeals correctly recognized and applied this rule. *See* Pet. App. at 10a. Respondent NCNB's argument that certiorari should be denied because of procedural defects in this case is a red herring, previously rejected by the Fifth Circuit, and should be similarly rejected by this Court.

Respondent NCNB goes far beyond claiming a procedural defect on Petitioners' part, however. Respodent claims that since Petitioners did not prove fraud in the district court their fraud claims are non-existent for the purposes of certiorari. Indeed it claims, "There is no evidence of a security, no evidence of fraud, no evidence of reliance by any Plaintiff." Opposition at 19. In fact, not only were the facts as stated by Petitioners necessarily taken as true by the district court, but Respondents themselves *admitted* many of Petitioners' factual claims in their First Amended Original Answer ("Answer"), including Petitioners' claims that they signed notes for stock purchases of Texas National Bank-Post Oak ("TNB-Post Oak") and Texas National Bank-Wstheimer ("TNB-Westheimer") with First RepublicBank Houston, N.A. ("RepublicBank"), the predecessor to NCNB; that RepublicBank financed the capitalization of TNB-Westheimer through a master note; and that directors of TNB-Westheimer and TNB-Post Oak brought suit against RepublicBank and others for fraud in the sale of the stock of TNB-Westheimer and TNB-Post Oak. Answer at 5. That Answer was, of course, part of the record for summary judgment purposes. Nor does Respondent stop with declaring the non-existence of fraud in this suit. It even

goes so far as to claim, "Petitioners' claims against the FDIC are *not* based on the sale of securities, because [First RepublicBank Houston] did not sell any of the stock in Texas National Banks, and Petitioners do not allege that it did." Opposition at 18. Not only is this new version of the facts belied by Respondents' own Answer, as shown above, but, in fact, Petitioners from the beginning of this case alleged that First RepublicBank was a seller of the securities Petitioners purchased in TNB-Westheimer and TNB-Post Oak, stating clearly in their First Amended Original Complaint,

> RepublicBank and Riddle engaged in the fraudulent sale of securities to Plaintiffs financed by loans from RepublicBank secured by bank stock. Therefore, RepublicBank and Riddle made each such sale to Plaintiffs under contracts made in violation of section 29.

Plaintiffs' First Amended Original Complaint at 32-33.

Having thus written off Petitioners' factual and legal securities fraud claims, Respondent proceeds to rewrite the facts it had formerly accepted, offering to this Court a version of the facts which it has never before presented in any pleading or in oral argument below. Opposition at 5-6. *This* attempt to sandbag Petitioners with a new version of the facts is the real procedural defect. Nevertheless, Respondents' rewriting of the facts and issues in this case—however improper—should not be allowed to obscure the real issue before this Court—which is the importance of granting certiorari to determine whether the Fifth Circuit Court of Appeals—in conflict with the Fourth, Sixth, Eighth, and Eleventh Circuit Courts of Appeals—was correct in holding that the federal common law *D'Oench, Duhme* doctrine shields the FDIC and the

successors to failed financial institutions from federal securities law claims.

CONCLUSION

For the foregoing reasons, Respondent NCNB's arguments against granting certiorari are without merit and the Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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No. 90-692

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In the Supreme Court of the United States

OCTOBER TERM, 1990

VICTOR ROGERS AND LOREN SINGLETARY,
PETITIONERS

v.

FEDERAL DEPOSIT INSURANCE CORPORATION,
AS RECEIVER FOR FIRST REPUBLICBANK HOUSTON,
N.A., AND NCNB TEXAS NATIONAL BANK

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly held that petitioners may not bring claims against the Federal Deposit Insurance Corporation and the successor to a failed bank based on alleged violations of the federal securities laws by the officers of the closed bank.

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BRIEF FOR THE FEDERAL RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-24a) is reported at 907 F.2d 1523. The opinion of the district court (Pet. App. 25a-30a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on July 25, 1990. A petition for rehearing was denied on August 21, 1990. Pet. App. 31a-32a. The petition for a writ of certiorari was filed on October 24, 1990. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioners are investors who executed promissory notes in favor of First RepublicBank, Houston, N.A. (FRB), a financial institution that is now insolvent. Petitioners contend that the promissory notes are invalid because they were obtained by FRB through fraud in violation of the federal securities laws.

More specifically, petitioners allege that, beginning in 1983, FRB assisted John C. Riddle and Jeffries C. Suttles, who were heavily indebted to FRB, in a scheme to defraud investors. FRB helped the two men open two branch banks of Texas National Bank (TNB) by lending investors, including petitioners, money for the purchase of TNB stock. The investors executed promissory notes in favor of FRB, thereby allowing FRB to acquire new collateral for the debts owed to it by Riddle and Suttles. Petitioners contend that FRB never told them that the TNB stock was subject to a voting trust giving control of the stock to Riddle and Suttles. They further assert that FRB encouraged and financed large TNB stock purchases, including their purchases, knowing that the stock was overvalued and that the TNB branch banks were doomed to fail. Pet. App. 2a-3a.

In 1987, Riddle and Suttles defaulted on their note for the purchase of one of the TNB branch banks, and both TNB branch banks failed shortly thereafter. In May 1988, petitioners, as stockholders of the TNB branch banks, filed this federal securities fraud action in a federal district court against Riddle, Suttles, and FRB.[1] In July 1988, FRB also

[1] The FDIC, as receiver for one of the failed TNB branches, participated in other litigation involving the TNB branches and FRB. Pet. App. 3a.

failed, leading to the appointment of the FDIC as its receiver. The FDIC subsequently sold some of FRB's assets, including petitioners' promissory notes, to respondent North Carolina National Bank—Texas (NCNB). The FDIC and NCNB were then substituted as defendants in place of FRB in this case.

The FDIC and NCNB filed counterclaims against petitioners seeking enforcement of the promissory notes and moved for summary judgment. The FDIC and NCNB claimed that the federal common law doctrine set forth in *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942), and later cases, barred petitioners' securities fraud claims. In addition, the FDIC and NCNB contended that the rule of *D'Oench* barred petitioners' defenses against enforcement of their notes. The district court granted summary judgment in favor of the FDIC and NCNB. Pet. App. 25a-30a.

2. The court of appeals affirmed. Pet. App. 1a-24a. It found this Court's recent decision in *Langley* v. *FDIC*, 484 U.S. 86 (1987), particularly instructive. In that case, decided under *D'Oench*'s statutory counterpart, 12 U.S.C. 1823(e),[2] the Court rejected

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[2] 12 U.S.C. 1823(e) provides:

> No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this section or section 1821 of this title, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—(1) is in writing, (2) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution, (3) was approved by the board of directors of the depository institution or its loan committee, which approval shall be

the contention "that the word 'agreement' in [Section 1823(e)] encompasses only an express promise to perform an act in the future." 484 U.S. at 90. Rather, the Court held that the term also includes the representations and conditions that formed the basis of the bargain. *Id.* at 91. Accordingly, the Court in *Langley* rejected a claim that a mortgage was unenforceable by the FDIC because the bank that executed the mortgage had induced it by making fraudulent misrepresentations. The court below found that "[e]xcept for the fact that the asset in this case is stock rather than land, and its sale thus regulated by federal law, the cases are the same." Pet. App. 11a.[3] The court of appeals held that borrowers like petitioners "who execute facially unqualified obligations may not prevent a federal receiver's collection efforts by claiming that they were induced

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reflected in the minutes of said board or committee, and (4) has been, continuously, from the time of its execution, an official record of the depository institution.

[3] The court of appeals noted that this case was brought before Section 1823(e) was amended to protect the FDIC in its capacity as receiver. The court held that it did not have to decide whether that change in the statute applied in this case because "[t]here are two *D'Oench, Duhme* doctrines, one statutory (12 U.S.C. § 1823(e)) and one of common law," and the common law rule has long been applied to protect the FDIC in its capacity as receiver. Pet. App. 7a n.4. The court added that "[c]ourts often consider the *D'Oench, Duhme* doctrine and § 1823(e) in tandem." *Ibid.*, quoting *Beighley* v. *FDIC*, 868 F.2d 776, 784 (5th Cir. 1989). See also *Langley*, 484 U.S. at 92-93 (construing "agreement" in Section 1823(e) in light of *D'Oench*); *Olney Savings & Loan Ass'n* v. *Trinity Banc Savings Ass'n*, 885 F.2d 266, 274 (5th Cir. 1989) ("[a]s the aims of § 1823(e) and *D'Oench* are identical * * * the reasoning applied in § 1823(e) cases is applicable to *D'Oench* cases").

to execute the obligations by fraud." Pet. App. 9a-10a.

The court of appeals then explained in more detail why the fact that stock is involved in this case does not distinguish it from *Langley*. The court noted (Pet. App. 11a-12a) that it had previously rejected similar arguments based on state common law fraud claims in *Beighley* v. *FDIC*, 868 F.2d 776, 784 n.12 (5th Cir. 1989), and that the only court of appeals to decide the question had held in *FDIC* v. *Investors Associates X., Ltd.*, 775 F.2d 152, 156 (6th Cir. 1985), that claims based on the federal securities laws were also barred. Those decisions were correct, the court stated, because the basic principle underlying the *D'Oench* doctrine, "which is of particular relevance today," is that it is "federal policy to protect [the FDIC] *and the public funds which it administers* against misrepresentations as to the securities or other assets in the portfolios of the banks which [it] insures." Pet App. 13a, quoting *D'Oench, Duhme*, 315 U.S. at 457. The court added that "precluding this action does not deprive the plaintiffs of protection under the federal securities laws" since "[t]hey may sue the individuals who actually defrauded them." Pet. App. 12a-13a. In that connection, the court noted, while the federal government insures bank deposits, "there is no federal policy of protecting investors by the government underwriting of privately issued securities." *Id.* at 13a.[4]

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[4] Judge Brown dissented. In his view, *Langley* is distinguishable because petitioners do not allege fraud in the inducement. Pet. App. 18a. In addition, he contended that the other cases rejecting defenses based on state law were grounded on the principle that there is a need "for a uniform federal rule when dealing with the FDIC," a principle that

ARGUMENT

The court of appeals correctly applied settled principles of law in deciding this case, and its holding does not conflict with any decision of this Court or any other court of appeals. Moreover, the decision in this case has limited prospective importance in light of amendments to the federal banking laws. Further review is therefore not warranted.

1. The *D'Oench* doctrine and its statutory counterpart, 12 U.S.C. 1823(e), protect the FDIC from a bank's misrepresentations concerning its assets and from unrecorded side agreements that are not reflected in a bank's records. 315 U.S. at 457. In *D'Oench*, this Court specifically held that the maker of a promissory note cannot defend against the FDIC's enforcement of the note when the maker has "lent himself to a scheme or arrangement whereby the banking authority * * * was or was likely to be misled." *Id.* at 460. The doctrine has been " 'extended considerably by the courts' since the 1942 decision." *Beighley*, 868 F.2d at 784. As the court of appeals stressed, in *Langley* this Court held that a misrepresentation to borrowers concerning a condition under which a loan is made constitutes fraud in the inducement, and a borrower may not defend against enforcement of the agreement in an action brought by the FDIC on the basis of such misrepresentations. 484 U.S. at 93-94. In addition, in light of this Court's decision in *Langley*, the courts of appeals have repeatedly held under the common law rule of *D'Oench* that a bank's misrepresentations to borrowers cannot be asserted as a defense to recovery by

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is inapplicable in a case involving allegations of violations of the federal securities laws. *Id.* at 23a.

federal authorities on facially unqualified notes. *McLemore* v. *Landry*, 898 F.2d 996, 1002 (5th Cir.), cert. denied, 111 S. Ct. 428 (1990); *FSLIC* v. *Lafayette Investment Properties, Inc.*, 855 F.2d 196, 198 (5th Cir. 1988); *FSLIC* v. *Murray*, 853 F.2d 1251, 1255 (5th Cir. 1988). And as the court of appeals noted in its opinion, the Sixth Circuit held that *D'Oench*'s bar to misrepresentation claims and defenses applies to "fraud in the inducement" arguments based on the federal securities laws. Pet. App. 11a-12a, citing *FDIC* v. *Investors Associates X. Ltd.*, *supra*.

Petitioners contend (Pet. 9) that *Langley* is inapplicable because they do not allege fraudulent inducement. However, the factual predicate of their claim, as presented in their petition (Pet. 5), is that FRB—knowing that the TNB stock was overpriced and eroding in value—nevertheless encouraged and financed petitioners' purchase of TNB stock. The obvious import of such an allegation is that FRB fraudulently induced petitioners to purchase TNB stock by withholding critical information. As the court of appeals observed, except for the fact that the asset in this case is stock rather than land, petitioners have asserted a fraud in the inducement action essentially indistinguishable from that barred under *Langley*. Pet. App. 11a.[5]

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[5] Petitioners further argue (Pet. 10-11) that their claim should be analogized to fraud in the factum because it is based on the federal securities laws, which provide that agreements are "void" rather than "voidable" in certain circumstances. Similar attempts to cloak a fraud in the inducement claim in the guise of a fraud in the factum claim have been given short shrift by the courts, which have properly looked to the facts of the case. For example, in *McLemore* v. *Landry*, the Fifth Circuit held that where borrowers had

Petitioners also contend (Pet. 12-15) that because their claim is based on the express statutory provisions of the federal securities laws, resort to federal common law doctrines such as *D'Oench* is precluded. This Court, however, has recently held that common law defenses may be available in limited situations to defeat express and implied statutory securities fraud claims. *Pinter* v. *Dahl*, 486 U.S. 622, 633-639 (1988); *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 306-311 (1985).

More to the point, petitioners' argument is mistakenly premised on the claim that the body of law related to its fraud claim is limited to investor rights under the federal securities laws. But the question presented also relates to what powers are available to the FDIC, as successor to an insolvent financial institution, in disposing of claims formerly made against the institution. Congress has enacted a comprehensive legislative scheme to provide the FDIC with broad remedial powers as the successor to failed institutions, and all persons with claims against insolvent institutions must look to this scheme to determine their rights and duties. *Unisys Corp.* v. *FDIC*, 724 F. Supp. 454, 457 (W.D. Tex. 1988); *In re American City Bank & Trust Co., N.A.*, 402 F. Supp. 1229, 1231 (E.D. Wis. 1975); see also *Cook County Nat'l Bank* v. *United States*, 107 U.S. 445, 448 (1883). And that legislative scheme has consistently been interpreted in light of this Court's decision in *D'Oench, Duhme*, which retains independent force. See note 3, *supra*.

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knowledge of the character or terms of the loan document, fraudulent misrepresentations that induced borrowers into signing for the loan fell within the scope of *Langley*. 898 F.2d at 1002; see also *FSLIC* v. *Murray*, 853 F.2d at 1255.

In addition, Congress has recently augmented the federal laws governing financial institutions by enacting the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA), Pub. L. No. 101-73, §§ 212, 214, 217, 103 Stat. 183, 231, 249, 256-257 (1989). In FIRREA, Congress made clear that claims such as those advanced by petitioners are not valid against the FDIC or bridge banks like NCNB. It did so by providing that Section 1823(e) applies when the FDIC acts as a receiver; by adding 12 U.S.C. 1821(d)(9)(A), which provides that "any agreement which does not meet the requirements set forth in section 1823(e) of this title shall not form the basis of, or substantially comprise, a claim against the receiver or the Corporation"; and by enacting similar protections for bridge banks in 12 U.S.C. 1821(n)(4)(I). There is no exception to these provisions for claims based on federal laws. Since under *Langley* petitioners' fraudulent inducement claims constitute part of their "agreement," but the fraudulent statements were not recorded, their defenses against the FDIC are barred by Section 1823(e). Similarly, their causes of action against the FDIC are barred by Section 1821(d)(9)(A) because "the basis" of their claim is the unrecorded fraudulent inducement. And NCNB has similar protections under Section 1821(n)(4)(I).[6]

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[6] Although the court of appeals decided not to reach the issue (Pet. App. 7a n.4), these protections may be applied in a pending case like this one. FIRREA §§ 212, 217, 103 Stat. 231, 256; *Bradley v. Richmond School Board*, 416 U.S. 696, 715 (1974); *FDIC* v. *Kasal*, 913 F.2d 487, 493 (8th Cir. 1990).

2. Petitioners mistakenly assert (Pet. 15-20) that the decision of the court of appeals conflicts with the holdings of other courts of appeals.

Three of the cases cited by petitioners as presenting a conflict are clearly inapposite. In *Gilman* v. *FDIC*, 660 F.2d 688, 693-695 (1981), the Sixth Circuit ruled in favor of the FDIC and did not even address the issue raised by petitioners.[7] Similarly, in *FDIC* v. *Aroneck*, 643 F.2d 164 (4th Cir. 1981), the FDIC did not even raise the rule of *D'Oench*. And in *Astrup* v. *Midwest Federal Savings Bank*, 886 F.2d 1057, 1059-1060 (1989), the Eighth Circuit held that while *D'Oench* affords no protection against tort claims, it does preclude recovery on the basis of agreements that contradict the records of the insolvent institution. As this Court recognized in *Langley*, a fraudulent inducement claim is premised on an undisclosed agreement or condition (484 U.S. at 93), and such a claim is therefore based on contract, not tort. In this case, like *Langley*, petitioners' claim is based on unrecorded representations that allegedly induced petitioners to enter into a contract.[8]

Petitioners also claim that two decisions of the Eleventh Circuit, *Gunter* v. *Hutcheson*, 674 F.2d 862,

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[7] Moreover, in its later decision in *FDIC* v. *Investors Associates X., Ltd.*, 775 F.2d at 155-156, the Sixth Circuit expressly rejected federal securities law defenses on the basis of the *D'Oench* doctrine.

[8] Petitioners also assert (Pet. 16) that the decision of the court of appeals conflicts with this Court's decision in *Oppenheimer* v. *Harriman Nat'l Bank & Trust Co.*, 301 U.S. 206 (1937). However, the decision in *Oppenheimer* predates this Court's decision in *D'Oench*, and the case did not involve, nor did this Court address, the protections afforded the FDIC as successor to a failed financial institution. See Pet. App. 5a n.3.

cert. denied, 459 U.S. 826 (1982), and *Vernon* v. *Resolution Trust Corp.*, 907 F.2d 1101 (1990), support its position. However, in *Gunter* the Eleventh Circuit held that the FDIC had a defense under the federal securities laws to the plaintiffs' claims and affirmed the dismissal of those claims on that independent basis. 674 F.2d at 874-877. Similarly, in *Vernon* the Eleventh Circuit affirmed the dismissal of claims against a financial institution that had entered into a purchase and acquisition agreement with the Federal Savings and Loan Insurance Corporation on the basis of the terms of the agreement. 907 F.2d at 1108. Accordingly, the Eleventh Circuit's comments with respect to the rule of *D'Oench* were not necessary to its holdings.[9]

3. Finally, review is not warranted since the question presented has a relatively limited impact. First, as the prior discussion of the decisions of other courts of appeals shows, the FDIC has a variety of defenses available to it in cases like this other than the rule of *D'Oench*. Thus, as the dissenting judge stated, "[i]n the vast majority of cases" plaintiffs such as petitioners would not prevail in any event. Pet. App. 24a.

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[9] Moreover, the decision in *Gunter* preceded this Court's decision in *Langley*, and the Eleventh Circuit's conclusion that certain fraudulent representations were not part of the relevant "agreement" within the meaning of Section 1823(e) is contrary to this Court's conclusion (484 U.S. at 90-91) that "agreement" includes the representations and conditions made in connection with the bargain. In *Vernon*, the Eleventh Circuit distinguished a number of decisions on the ground that they involved "the validity and enforceability of a particular debt or monetary obligation," such as "a promissory note." 907 F.2d at 1107. This case is accordingly distinguishable under the logic of the court since the enforceability of promissory notes is at issue.

Second, even if the recent amendments to the federal statutes governing financial institutions are not applicable in this case (see note 6, *supra*), they resolve the issue prospectively.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JANUARY 1991

☆ U. S. GOVERNMENT PRINTING OFFICE: 1991 282061 20310